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No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

WALTER PODROG AND J. FRANK MANNING,
Class Representatives, Grand Junction Bondholder Class
(Fabricating, Inc.)
Petitioners,

VS.

WARING, COX, JAMES, SKLAR & ALLEN,
Attorneys, a partnership,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF TENNESSEE

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QUESTION PRESENTED

Was it not a violation of the Equal Protection Clause of the Fourteenth Amendment of the U. S. Constitution for the Supreme Court of Tennessee to hold that an action against an attorney based on a violation of the Tennessee municipal securities fraud statute was time-barred after one (1) year, since, under Tennessee law, a similar action against a non-attorney based on the same statutory violation would not be time-barred for a longer period of time (three (3) years).

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Attorneys, a partnership,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF TENNESSEE

Walter Podrog and J. Frank Manning, representatives of the Bondholder Class, petition for writ of certiorari to review the judgment of the Supreme Court of Tennessee in this case.

OPINIONS BELOW

The Opinion of the Supreme Court for Tennessee (App. A,infra, pp. A1-A12) and its denial of the Petition to Rehear (App. B, infra, pp. A13-A16) are reported at 673 S.W.2d 860 (Tenn. 1983). The opinions of the Tennessee Court of Appeals (Western Section) (App. D, infra, pp. A33-A52) and of the Chancery Court of Hardeman County, Tennessee (App. C, infra, pp. A17-A32) are not and will not be reported.

JURISDICTION

The judgment of the Supreme Court of Tennessee (App. A, infra pp. A53-A54) was filed on December 19, 1983. The Class'petition for a rehearing was denied on July 9, 1984. (App. B, infra pp. A13) The jurisdiction of this Court is invoked under 28 U.S.C. 1257(3).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

1. The Fourteenth Amendment to the United States Constitution provides in relevant part:

> "...nor shall any state ... deny to any person within its jurisdiction the equal protection of the laws."

2. Section 9-1402 of the Tennessee Code Annotated, titled The Tennessee Municipal Securities Act of 1972 [Acts of 1972 (adj. S.) ch. 765, §1.] (App. H., infra, A69-A70) provides in relevant parts:

> **Definitions.-**
>
> "(f) 'Fraud', 'deceit', and 'defraud' are not limited to common law deceit.
>
> "(g) 'Prohibited Practices': The following shall be prohibited practices and shall be unlawful under the terms of this chapter:
>
> * * *
>
> "(2) For any person, in connection with any transaction or transactions in the state which involve any offer to sell or to buy municipal securities, or any sale or purchase of municipal securities, or advising municipalities with regard to financing municipal projects, either directly or indirectly, ... (b) *to engage in any act, practice, transaction or course of business which operates or would operate as a*

fraud or deceit upon the purchaser or seller, or the municipality." (emphasis added)

[Note: No limitation of actions is fixed in the statute itself.]

3. The relevant Tennessee limitation of actions statutes provide in pertinent parts as follows:

"...[A]ctions and suits *against attorneys for malpractice* whether said actions are grounded or based in contract or tort . . . shall be commenced within *one (1)* year after cause of action accrued..." Tenn. Code Ann. § 28-304 [Shown in its entirety at App. I, infra, p. A74] (emphasis added)

"Actions for *injuries to personal . . . property* . . . when no other time of limitations is fixed by the statute creating such liability . . . shall be commenced within *three (3) years* from the accruing of the cause of action. Tenn. Code Ann. §28-305 [Shown in its entirety at App. I, infra, p. A74] (emphasis added)

The Tennessee Supreme Court in *Vance v. Schulder* (Tenn. 1977) 547 S.W.2d 927, a securities fraud case, held that the three year statute of limitation to be the applicable statute, ruling that the damages resulting from securities fraud constitute an "injury to personal property".

STATEMENT OF THE CASE

A. The Material Facts

This case had its genesis in an industrial revenue bond issue sold by the Town of Grand Junction, Tennessee, in October and November, 1972.

Jerald H. Sklar, a partner in the law firm of Waring, Cox, James, Sklar and Allen (the Sklar firm), the respondents herein, was bond counsel; in addition he prepared the offering circular, and performed other underwriting functions in connection with the issue.

The issue went into default in October, 1974. In February, 1975, the Trustee Bank, joined by the Town, commenced this action in the Chancery Court for Hardeman County, Tennessee on behalf of the bondholders against the Company (Fabricating, Inc.) and the guarantors of the lease payments (Charles E. Bruce and E. C. Holman).

Somewhat later, the Trustee Bank and the Town sought and secured permission to file a Second Amended Complaint. This pleading created a "defendant class" composed of all the bondholders and sought a declaratory judgment of judicial exoneration in favor of the Trustee Bank, the Town, all attorneys, and all others involved.

By the time this case was tried in August, 1979, the alignment of the parties had changed totally. The Bondholder Class had become a plaintiff class; a settlement between the Class and the Trustee Bank had been approved by the Chancellor; the guarantors had been dismissed [following a judgment against them in litigation in the U.S. District Court at Dallas in favor of the Trustee for the bondholders in the amount of $1,488,650.32 (of which only a small percentage was collectable)]; and the Sklar firm and others were cast as defendants.

The Class' claims against the Sklar firm as a defendant were based on both common-law negligence and on the violation of the T.C.A. 1402(g)(2)(b).

The trial court found in favor of the Class and against the Sklar firm on *both* counts, and entered judgment against said firm in the amount of $505,768.28.

The Tennessee Court of Appeals reversed on the grounds that both of the Class' claims were time-barred, saying (at p. 11 of its Opinion):

> "We hold that the counterclaim of the bondholder class seeking relief against the Sklar firm based upon common law negligence *and the violation of T.C.A. § 9-1402 (g)*

> [The 1972 Act] is barred by the one-year statute of limitations as set out in T.C.A. § 28-304." (emphasis added)
>
> (App. D, infra, pp. A43-A44)

Said Opinion did not allude to or discuss the Class' argument that since said 1972 Act contained no "built-in" limitation of actions provision, under the aforementioned 1977 holding of the Tennessee Supreme Court in *Vance v. Schulder*, 547 S.W.2d 927, the three year statute (T.C.A. §28-305) should be the governing statute as to the claim based on the violation of the statute. This argument, of course, is based on the simple premise that the same statute of limitations for the violation of a statute should appiy to attorney-violators and non-attorney violators alike.

The Supreme Court of Tennessee granted the Class a limited appeal from the Court of Appeals' decision, limited to the statute of limitation questions. In its Opinion rendered December 19, 1983, the Tennessee Supreme Court affirmed the Tennessee Court of Appeals' decision that the Class' action against the Sklar firm for violation of the 1972 Act (as well as its common law negligence action) was governed by the one-year attorney malpractice statute, and on July 9, 1984, it denied the Class' petition to rehear.

B. The Raising Of The Federal Question

The federal question here presented was specifically raised in the written briefs and arguments filed with the Supreme Court of Tennessee and also in the oral argument before that Court on April 6, 1982.

At all times, the Class has contended that the one-year "attorney malpractice" statute (T.C.A. § 28-304, App. I, infra, p.A74) applied *only* to the common-law negligence claim, *and that the three year "injury to personal property" statute (T.C.A. § 28-305, App. I, infra, p. A74) applied to the claim based on violation of the Tennessee Municipal Securities Act of*

1972 [T.C.A. § 9-1402(g)(2)(b)], since both attorneys and non-attorneys can and do violate securities fraud statutes.

The Class made no direct reference to the federal question in the lower courts or in its briefs filed therein since the issue did not arise until the Tennessee Court of Appeals held that both claims (i.e. the common law negligence claim and the statutory violation claim) were time-barred by the one-year attorney malpractice statute.

The specific references in the Class' briefs and arguments to the Supreme Court of Tennessee to the federal constitutional questions are as follows:

1. In the Class' Principal Brief (at p. 23):

> [A holding which applies a shorter statute of limitations to an attorney than to a non-attorney for a violation of the same statute] "...offends our traditional notions of fair play and substantial justice; furthermore such a holding constitutes a violation of the Equal Protection Clause of the United States Constitution, ... The late Justice Henry, speaking for this Court, wrote:
>
> > '[1] The phrase 'equal protection', as used in the Fourteenth Amendment to the Constitution of the United States, requires that all persons and entities shall be treated the same under like circumstances and conditions, both as to privileges conferred and liabilities incurred.'
> >
> > *Genesco, Inc. v. Woods* (Tenn. 1979) 578 S.W.2d 639, at 641"

2. In the Class' Supplementary Argument (App. F, infra, pp. A55-57), filed with the Tennessee Supreme Court on August 8, 1983, for the specific purpose of calling the Tennessee Supreme Court's attention to

this Court's June 6, 1983 Opinion, in the case of *Pickett, et al v. Brown, et al* ____ US ____ 76 L Ed 2d 372, wherein a Tennessee statute of limitations was invalidated on the grounds that it violated the Equal Protection Clause of the Fourteenth Amendment, the Class argued that the rationale of *Pickett* applied to this case, and that it required the Tennessee courts to hold that since under *Vance v. Schulder* (Tenn. 1977) 547 S.W.2d 927, a non-attorney could be sued within a three (3) year period following a violation of T.C.A. § 9-1402(g)(2)(b), an attorney could also be sued within said three (3) year period for a similar violation of said statute.

3. In the Class' Petition to Rehear, filed with the Tennessee Supreme Court, reference was again made to the ". . . constitutional problems dealt with in the Supplementary Argument".

The Tennessee Supreme Court has therefore repeatedly been confronted with this federal constitutional question, but has steadfastly refused to deal specifically and/or directly with it, despite the Class' respectful insistence that it do so.

REASONS FOR GRANTING THE PETITION

The Tennessee Supreme Court, by its decision in this case, has grafted a judicially created amendment on to the three year "injury to personal property" statute of limitations (T.C.A. § 28-305, App. I, infra, p. A74) reading substantially as follows:

> "provided, however, if the defendant is an attorney, the one-year attorney malpractice statute shall govern, even though the wrongful act constitutes a violation of a statute which is subject to being violated by both attorneys and non-attorneys".

This judicial graft, if permitted to stand, will constitute a flagrant violation of the Equal Protection Clause of the Four-

teenth Amendment; it represents an unreasonable and arbitrary classification, and serves no sound public policy; it is doubly offensive in that it constitutes a judicial grant of a special defense to attorneys [who are, of course, "insiders" in the administration of justice in this nation] - namely, the defense of a short one-year statute of limitations, not available to non-attorneys.

This judicially created classification which applies the one year statute to attorneys and the three year statute to non-attorneys for the same violation of a statute prohibiting securities fraud lacks a reasonable and justifiable basis, since both attorneys and non-attorneys can and do violate securities fraud statutes.

CONCLUSION

The assault on the integrity of the Equal Protection Clause which this case represents is especially insidious and offensive since it favors "insiders" to our judicial system. This Court should use this case to make it clear to the judiciary, the bar, and the public that it will not permit Tennessee or any other state to give favored and unwarranted treatment to its attorneys in its system of laws.

Respectfully submitted,

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APPENDIX

APPENDIX A

IN THE SUPREME COURT OF TENNESSEE
AT JACKSON

Security Bank & Trust
Company of Ponca City,
Oklahoma, and the Town
of Grand Junction, Tennessee,
Plaintiffs,

v.

Fabricating, Inc., E. C.
Holman and Charles E. Bruce,

and

Walter Podrog, L. J. Perry,
J. W. Caperton, Union Planters
National Bank, and all known
Bondholders of Town of Grand
Junction Bonds Date October 1,
1972,
Defendants.

and

J. Frank Manning and Walter
Podrog, Representatives of
the Class of Bondholders of
Town of Grand Junction Bonds,
Dated October 1, 1972
(Fabricating, Inc.),
Counter-Plaintiffs-
Appellants,

v.

The Above named Plaintiffs
and Waring, Cox, James, Sklar
and Allen, a Partnership

composed of Allen Cox, Jr., Roane Waring, Jr., Erich William James, Robert Lee Cox, Jerald H. Sklar, Lewis F. Allen and Roger D. Fish, as General Partner,

Counter-Defendants-Appellees.

Appeal from the Court of Appeals

Appeal from the Chancery Court for Hardeman County

Hon. William H. Inman, Chancellor, Sitting by Designation

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Agnes Thornton Bird
Frank B. Bird
Maryville

Of Counsel:
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For Appellees:

Leo Bearman, Jr.
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Of Counsel:

Heiskell, Donelson, Bearman Adams, Williams & Kirsch
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OPINION

Affirmed. Brock, J.

As the parties are presently aligned, this is a class action brought by representatives of a class of bondholders of the Town of Grand Junction, Tennessee, against the law firm of Waring, Cox, James, Sklar & Allen for damages resulting from alleged malpractice.

A judgment was rendered in favor of the bondholders against the Waring firm and against the Town of Grand Junction in the Chancery Court for Hardeman County, but the judgment against the Waring firm was reversed by the Court of Appeals, as was the judgment against the Town of Grand Junction, and the cause was dismissed as to both defendants. We granted the application of the bondholders for an appeal from the judgment of the Court of Appeals, limited to a consideration of the "issues that relate to the statutes of limitation as they may apply to the class' actions against the law firm of Waring, Cox, James, Sklar & Allen."

I

This controversy arose out of the issuance of industrial revenue bonds by the Town of Grand Junction, Tennessee, for the purpose of financing the construction of a manufacturing plant to build modular motel rooms. Half of the bonds were issued in October, 1972, and the other half were issued in November, 1972; their default occurred on October 1, 1974.

The Mayor of Grand Junction, Carl Dunn, Jr., had been contacted by Charles Bruce, a former resident of Grand Junction who had moved to Texas. It appears that Bruce was an old friend of the Dunn family and enjoyed a good reputation in Grand Junction. Bruce and his partner, E. C. Holman, proposed to form a corporation to be known as Fabricating, Inc., which would operate the above mentioned manufacturing plant

on land leased from the Town of Grand Junction; the whole venture was to be financed through the proposed issuance of industrial revenue bonds by the Town, the bonds to be repaid through rents received by the Town from the proposed corporation lessee. Bruce and Holman proposed to, and did, personally guarantee the bond issue and in support of these guaranties submitted financial statements of their personal estates and financial condition which purported to have been prepared by Lester H. Centu, a Certified Public Accountant.

The Town of Grand Junction employed Mr. Jerald Sklar, an attorney with the law firm of Waring, Cox, James, Sklar & Allen, to serve as special bond counsel to the Town for the purpose of passing upon the legality and non-taxability of the proposed bond issue, for the preparation of the lease to Fabricating, Inc., and a trust indenture and, of special interest in this litigation, for the preparation of the offering circular which was employed in the issuance and merchandising of the bond issue. The Security Bank & Trust Company of Ponca City, Oklahoma, served as trustee under the revenue bond issue and, as such, held the funds received from the bond issue and disbursed them as the plant was built.

The purported financial statements of Bruce and Holman were attached to the offering circular used in the promotion of the bond issue.

The bond coupons falling due on October 1, 1974, defaulted.

It was learned that Bruce and Holman did not have the assets reflected on their financial statements and that Lester Centu was not a Certified Public Accountant.

One of the holders of the defaulted bonds was Walter Podrog of Palm Beach, Florida, who possessed a law degree and was experienced in both general obligation and revenue bonds. As the owner of $10,000.00 worth of the defaulted bonds, Mr. Podrog began a personal investigation into the reasons for the default.

He contacted the defendant attorney Jerald Sklar, Charles Johnson, the attorney for the Trustee bank, Larry Stephenson, President of the bank, and Mayor Dunn and others. On May 15, 1975, Mr. Podrog wrote a letter to attorney Charles Johnson in which he contended that the Town, the Mayor, the council, the law firm of Waring, Cox, James, Sklar & Allen, and other were aware of the true character of the guarantors, Bruce and Holman, but had failed to check into their financial statements, much to the serious detriment of the bondholders. Then, on July 21, 1975, Mr. Podrog wrote a letter to the Trustee bank recommending that civil suit be instituted on behalf of all bondholders against the Town, the Mayor, the council, the law firm of Waring, Cox, James, Sklar & Allen, Ewing Harris, the general counsel for the Town of Grand Junction, Tennessee, and the underwriters of the bond issue for causing the loss suffered by the bondholders. Still later, on September 30, 1975, Mr. Podrog wrote a letter to all bondholders in which he stated:

> "The correspondence, telephone calls and inquiries, including a personal visit to Grand Junction, convinced me that this ill-fated promotion was fraudulently inspired from the start. All involved in the promotion and ultimate sale of bonds were at least negligent in permitting false financial statements and apparent forged CPA certifications to be publicized and circulated as true. One of the guarantors was Mayor Dunn's employer and presently is a partner in the Tennessee Pewter Company being operated in a portion of subject premises. An apparent $300,000.00 windfall profit was made by guarantors and/or others.
>
> * * *
>
> "After the total losses of bondholders is determined, civil action for damages should be filed against the Town of Grand Junction, its Mayor, its council, the original underwriters and all attorneys involved in their promotion and sale of the bonds, to the purchasers, due to the carelessness and negligence in permitting fraudulent negligent statements to be published and circulated."

The original complaint in this action was filed on February 10, 1975, in the Chancery Court by the Security Bank & Trust Company of Ponca City, Oklahoma, and the Town of Grand Junction, Tennessee, plaintiffs, against Fabricating, Inc., a corporation, and E. C. Holman and Charles E. Bruce, the two guarantors of the industrial revenue bonds issued by the Town of Grand Junction, dated October 1, 1972, and November 1, 1972. This complaint sought reimbursement of monies due the Bank as trustee of the bond issue when the issue failed and guarantors refused to make good on their guaranty. This original complaint was amended twice and in the second amended complaint filed on November 24, 1975, the bondholders were named defendants, as a class, and the Trustee Bank sought a declaratory judgment that the actions taken by the Bank, its agents, its attorneys and employees in administering and controlling the bond trust assets and estate had been proper and lawful.

Bondholder Podrog filed an individual answer to this second amended complaint on January 6, 1976, but did not file any counter, cross, or third-party complaint at that time. Bondholders, J. Frank Manning and Walter Podrog, were appointed representatives of the class of bondholders and, as such, filed an answer to the second amended complaint and also filed a third-party complaint against the defendant law firm, Waring, Cox, James, Sklar & Allen, and the members thereof alleging various acts of negligence on the part of Mr. Sklar in performing his duties as bond counsel with respect to the bond issue and particularly with respect to the offering circular which was published and circulated to assist in promoting the sale of the bonds. The primary allegation was that Mr. Sklar should have discovered the falsity of the financial statements of the promoters and guarantors of the bonds, that Mr. "Centu" was not a CPA, that the underwriters of the bond issue in question were under investigation by government agencies with respect to their activities in connection with other securities and that Mr. Sklar's failure to discover and disclose these and other deficien-

cies was a direct and proximate cause of the loss suffered by the bondholders. The date of the filing of this cross-action against the Sklar firm was November 24, 1976.

At the same time the bondholder class filed a counterclaim against the Security Bank & Trust Company of Ponca City, Oklahoma..

The original suits brought by the Trustee Bank and the Town of Grand Junction against Fabricating, Inc., and the promoters and guarantors, Bruce and Holman, were dismissed. A different suit was filed against Bruce and Holman in Texas in an effort to enforce their contract of guaranty of the bonds. Prior to the trial in the instant cause, the Security Bank & Trust Company of Ponca City, Oklahoma, settled its liability with the bondholder class for a total of $250,000.00 which was approved by the Chancery Court.

Eventually, all that remained for trial was the claim of the bondholder class against the bond attorneys and the Town of Grand Junction, Tennessee. In addition to the claim of malpractice made against bond counsel, the bondholder class alleged that bond counsel and the Town of Grand Junction had violated the Tennessee Municipal Securities Act of 1972, T.C.A., § 9-1401 *et seq.*

The Chancellor found the issues in favor of the bondholder class and awarded a decree in its favor against the defendant attorneys and the Town of Grand Junction in the amount of $491,000.00 plus interest, making a total judgment of $505,716.78.

The Court of Appeals reversed the decree of the Chancellor and dismissed the action of the bondholders, concluding that, with respect to bond counsel, the bondholders' action was barred by the statute of limitations stated in T.C.A., § 28-3-104, which requires that "actions against attorneys for malpractice" must be brought within one year of the accrual of the cause of

action and concluding further, with respect to the Town of Grand Junction, that the evidence failed to show that the Town had violated the provisions of the Tennessee Municipal and Securities Act of 1972, T.C.A., § 9-1401, *et seq.*

This Court granted the application of the bondholder class to appeal, limited to a consideration of the issues concerning the defense of the statute of limitations which had been sustained by the Court of Appeals.

Clearly, the cause of action asserted against the defendant attorneys is one for malpractice in the performance of their duties as bond counsel; thus, the statute of limitations to be applied is that contained in T.C.A., § 28-3-104, which provides:

> ". . . actions and suits against attorneys for malpractice whether said actions are grounded or based in contract or tort, . . . shall be commenced within one year after cause of action accrues."

See, Ameraccount Club, Inc. v. Hill, Tenn., 617 S.W.2d 876 (1981).

When was this action commenced?

We hold that the action of the bondholder class was not commenced until November 24, 1976, the date of the filing by the bondholders of their third-party complaint against the defendant bond attorneys. Until they were brought in by service of process under the third-party complaint, the third-party defendant attorneys were not parties to the action; therefore, the argument of the bondholders that the running of the statute of limitations was tolled by the filing on January 9, 1976, by bondholder Podrog of his individual answer to the second amended complaint filed by the original plaintiffs in which he made generalized claims for relief against the original plaintiffs, cannot be sustained; Podrog's individual answer cannot be construed as asserting any claim whatever against bond counsel because they were not parties, plaintiff or defendant, at that time.

Bond counsel did not become real parties in interest merely by acting as counsel for the Security Bank & Trust Company in the filing and prosecution of the second amended complaint which sought a declaratory judgment against the bondholder class exonerating the Bank, its original counsel, Phipps, Johnson & Holmes, and the Bank's other employees of any liability arising out of the administratin of the trust fund consisting of the proceeds derived from the sale of the bonds. Bond counsel did not represent the Bank in the administration of the trust fund and had no interest, *as parties,* in the outcome of that case. Bond counsel's only interest was that of attorneys representing their client. *Cf. Tennessee Eastman Company v. Adams,* 214 Tenn., 451, 381 S.W.2d 269 (1964). In the *Tennessee Eastman Company* case this Court recognized that one who is not a party to litigation may, by reason of its control of the proceedings and its financial interest in the outcome thereof, become a real party in interest and, therefore, bound by the judgment rendered therein. Here, however, bond counsel did not have such interest and control in the second amended complaint.

The result is that since bond counsel were neither named parties nor "real parties in interest" at the time Mr. Podrog filed his answer to the second amended complaint on January 9, 1976, the filing of that answer did not toll the running of the statute of limitations in their favor.

When did this cause of action accrue?

We now consider whether or not the plaintiffs' cause of action accrued within one year of the filing of their third-party complaint on November 24, 1976. This Court has had occasion in several recently decided cases to consider various aspects of the problem of determining the date on which a plaintiff's cause of action has accrued sufficiently to start the running of the statute of limitations. *See, Teeters v. Currey,* Tenn., 518 S.W.2d 512 (1974); *McCroskey v. Bryant Air Conditioning Company,* Tenn., 524 S.W.2d 487 (1975); *Ameraccount Club,*

Inc. v. Hill, supra; Foster v. Harris, Tenn., 633 S.W.2d 304 (1982); *Hoffman v. Hospital Affiliates, Inc.*, Tenn., 652 S.W.2d 341 (1983).

In *Ameraccount* the action was one by a client against his attorney for malpractice in which we held that the statute did not begin to run until the injury to the plaintiff occurred, although he knew prior thereto of the attorney's negligence which eventually caused the injury. Obviously, negligence without injury is not actionable; hence, the statute of limitations could not begin to run until the attorney's negligence had resulted in injury to the plaintiff. In the instant case, the injury to the bondholders occurred on October 1, 1974, *when the bonds defaulted.* There is no merit whatever in the plaintiffs' argument that their injury did not occur until the suit against the guarantors in Texas was concluded. A plaintiff cannot be permitted to wait until he knows all of the injurious effects as consequences of an actionable wrong. *Taylor v. Clayton Mobile Homes, Inc.*, Tenn., 516 S.W.2d 72 (1974).

The date of injury to the bondholders being thus or in the exercise of reasonable care should have known, of the alleged negligence or malpractice on the part of bond counsel and of its causal relation to the injury suffered by the bondholders. The Court of Appeals concluded that the evidence showed that such knowledge was acquired no later than September 30, 1975, the date of Mr. Podrog's letter to all the other bondholders, a portion of which is hereinabove quoted. In that letter he asserts that ". . . all involved in the promotion and ultimate sale of bonds were at least negligent in permitting false financial statements and apparent forged CPA certificates to be publicized and circulated as true."

Earlier, in a letter dated July 21, 1975, Mr. Podrog had written to Mr. Larry Stephenson, President of the Security Bank & Trust Company, Ponca City, Oklahoma, wherein he stated:

> "I want to consult with them (all bondholders) and see if the majority agree with me that we should immediately:
>
> * * *

(5) institute civil suit for damages to all bondholders due to negligence, et cetera, against the Town of Grand Junction, its Mayor, its council, Waring, Cox, James, Sklar & Allen, Ewing J. Harris, Hamilton Brothers and Investors Associates of America for failing to verify guarantors' financial statements, et cetera, et cetera."

In his letter of September 30, 1975, to all of the other bondholders, Mr. Podrog has recommended:

> "After the total losses to bondholders is determined, civil action for damages should be filed against the Town of Grand Junction, its Mayor, its council, the original underwriters, and all attorneys involved in the promotion and sale of the bonds, to the purchasers due to the carelessness and negligence in permitting fraudulent financial statements to be published and circulated."

It is clear, then, that, at least as of September 30, 1975, the bondholders knew that they had sustained an injury and were aware of the existence of their claim for malpractice or negligence against bond counsel in failing to discover the fraudulent nature of the financial statements of the promoters-guarantors which were attached to the offering circular.

The bondholders argue that they were not aware of certain evidence of malpractice on the part of the bond counsel until they took Mr. Sklar's deposition in March, 1976. That may be, but, as we pointed out in *Hoffman, supra,*

> "The 'discovery' rule would apply only in cases where the plaintiff does not discover and reasonably could not be expected to discover that he has a right of action. Furthermore, the statute is tolled only during the period when the plaintiff has no knowledge that a wrong has occurred, and, as a reasonable person is not put on inquiry."
>
> *Hoffman v. Hospital Affiliates, Inc.*, 652 S.W.2d 341 at 344.

Plaintiffs have argued but have not proven that defendant bond counsel concealed plaintiffs' cause of action. Whatever plaintiffs learned upon the taking of Sklar's deposition in March, 1976, could have been learned much earlier if due diligence had been exercised by plaintiffs.

We have examined other complaints made by appellants-plaintiffs but find them to be without merit.

The judgment of the Court of Appeals is affirmed. Costs incurred in this Court are taxed against appellants-bondholders.

Ray L. Brock, J.

Cooper, Harbison, Drowota,
JJ., and Walker, Sp. J., Concur.

APPENDIX B

IN THE SUPREME COURT OF TENNESSEE
AT JACKSON

(Hardeman Equity)

Security Bank & Trust Company, et al.,
Plaintiffs,

v.

Fabricating, Inc., et al.,
Defendants,

v.

The Above Named Plaintiffs, Waring, Cox, James,
Sklar and Allen, et al.
Counter-Defendants.

OPINION ON PETITION TO REHEAR

I

The appellants (bondholder class) have filed a petition to rehear in this cause which we have considered and find to be without merit. Accordingly, the petition to rehear filed by the bondholder class is denied.

II

The appellees, the Sklar firm, have requested, pursuant to rule 40(d), T.R.A.P., that the Court authorize as an item of additional recoverable costs on appeal the premiums incurred by them for procuring and maintaining, while this case was in the appellate courts, premiums for a bond for stay of the judgment or decree rendered in the trial court. Appellees rely upon Rule 40(c), T.R.A.P., which provides:

> **"Recoverable costs on appeal**
>
> "Recoverable costs on appeal include the cost of preparing and transmitting the record, the cost of a transcript of the evidence or proceedings, the cost of producing necessary copies of briefs and the record, the premiums paid for bonds to preserve rights pending appeal, and any other fees of the appellate court or clerk."

This provision became part of our law for the first time on July 1, 1979, the effective date of the Tennessee Rules of Appellate Procedure. We are not aware of any court decisions construing it.

The bondholder class opposes this application for additional costs primarily upon the ground that the bond for stay was not necessary because the bondholder class at no time in this litigation has taken or threatened to take any action to enforce the judgment of the trial court pending appeal; they point out that

> "...since there are 140-plus members of the class, it would have been the height of folly for the class representatives to have sought to enforce the judgment and distribute the funds while an appeal was pending."

They further point out that even if there had been any necessity for a stay order at the time the original appeal was taken that necessity would have ended on February 3, 1981, the date of the judgment of the Court of Appeals reversing and setting aside the decree granted in the trial court in favor of the bondholder class.

Our research indicates that in other jurisdictions courts exercise discretion in considering whether or not, and to what extent, if any, an application for allowance of such premiums for stay or supersedeas bonds should be granted or denied. *See* Annot., 90 A.L.R.2d 448 (1963).

Rule 6 of the Tennessee Rules of Appellate Procedure *requires* that a bond for costs on appeal be filed by the appellant

in the trial court with the notice of appeal. That rule further provides that this bond shall be in the sum or value of $500.00 unless the trial court fixes a different amount. It is not necessary that an appellant file any other bond unless he desires to stay execution of the judgment rendered in the trial court, in which case, Rule 62 of the Tennessee Rules of Civil Procedure requires that a bond for stay be executed and filed. The right to appeal is not conditioned upon the filing of a bond for stay; but, if the appellant desires the protection of a stay, then the bond for stay must be filed. The pertinent provisions of Rule 62, Tennessee Rules of Civil Procedure, are as follows:

> "62.04 **Stay on appeal**
>
> "Except as otherwise provided in Rule 62.01, when an appeal is taken the appellant by giving a bond may obtain a stay. The bond may be given at or after the time of filing the notice of appeal. The stay is effective when the bond is approved by the court.
>
> "62.05 *Bond for stay*
>
> A bond for stay shall have sufficient surety and: (1) if an appeal is from a judgment directing the payment of money, the bond shall be conditioned to secure the payment of the judgment in full, interest, damages for delay, and costs on appeal;...."

One principle applied by courts in other jurisdictions is that only necessary disbursements may be allowed as taxable costs. *Christenson v. Cudahy Packing Co.*, 84 Cal. App. 237, 257 P. 906 (1927); *Giemza v. Allied American Mut. Fire Ins. Co.*, 10 Wis.2d 555, 106 N.W.2d 609 (1960); *Hackenjos v. Kemper Chevrolet Co.*, 193 Minn. 37, 257 N.W. 518 (1934), *petition for rehearing* 258 N.W. 433 (1935). In the *Christenson* case where the plaintiff recovered a money judgment and, on appeal, the judgment was modified to award costs to the defendant, it was held that the defendant could not recover the premium paid on a surety bond to stay execution of the judgment, since the

premium on such a bond was not a necessary expenditure within the meaning of the code section permitting recovery of such expenditures. Although the court in the *Giemza* case, *supra*, allowed a stay bond premium to be included as an item of recoverable costs, it clearly recognized the validity of the principle that in order for such a premium to be allowed as costs the appellant must show that the stay bond was reasonably necessary. Upon the facts there presented, the court rejected the contention of the appellee that the premium should not be recovered because the undertaking to stay execution was unnecessary, stating that it sufficiently appeared that the plaintiff-appellee's attorney had informed the defendant-appellant's attorney that execution would be issued if an appeal were taken, and that this was an adequate showing of need for an undertaking to stay execution.

We hold that before stay bond premiums should be awarded as recoverable costs on appeal under the authorization set out in Rule 40(c) of the Tennessee Rules of Appellate Procedure, the applying appellant should show that there was a necessity for obtaining a stay of execution pending the appeal. Since the requirement that necessity be shown had not been announced prior to the instant appellant's application for allowance of costs, we deem it just and proper to allow a further opportunity for the appellant to demonstrate such necessity and for the appellee class to demonstrate the lack of such necessity, by affidavits or otherwise. In accordance with the time schedule set out in Rule 40(d), T.R.A.P., the appellant is allowed fifteen (15) days from the filing of this opinion to file such proof as it desires and the appellee ten (10) days from receipt of appellant's proof in which to file opposing proof. A decision of this one issue will be deferred until such proof is submitted to the Court.

/s/ BROCK, J.

Cooper, C.J., Harbison and Drowota,
JJ., and Walker, Sp. J., Concur.

APPENDIX C

IN THE CHANCERY COURT OF HARDEMAN COUNTY, TENNESSEE

(Hardeman Equity)

Podrog, et al., and The Bondholder Class,
Plaintiffs,

vs.

Security Bank & Trust Company and
Town of Grand Junction, et al.
Defendants, Cross-Plaintiffs, Cross-Defendants.

MEMORANDUM OPINION

I

The Pleadings

This litigation began February 10, 1975, with the filing of a complaint by the Security Bank and Trust Company, a national bank of Ponca City, Oklahoma, and the Town of Grand Junction, Tennessee, against Fabricating, Inc., a Tennessee corporation doing business in Hardeman County, and E. C. Holman and Charles E. Bruce, officers and stockholders of Fabricating, Inc., and sometime Texas residents.

It was alleged that the plaintiff Town sold $1.2 million of industrial revenue bonds, and from the proceeds acquired land, constructed a manufacturing plant thereon and equipped it, and leased this property to Fabricating, Inc. on October 1, 1972. The plaintiffs alleged that the lease required semi-annual payments to the Trustee Bank, but that no payments were made, and formal default occurred October 1, 1974; that Bruce and Holman had guaranteed the payment of the rentals and were liable to the Trustee Bank therefor. Plaintiffs sought a judgment for the rent in arrears, together with the appointment of a Receiver for the "Project", as distinguished from the Corporation.

Carl Dunn, who was Mayor of Grand Junction, was appointed Receiver by Chancellor Summers on March 19, 1975, in a non-adversarial proceeding. The unilateral order describes him as a "responsible and qualified person".

Thereafter, the complaint was amended seeking the appointment of a Receiver for Fabricating, Inc., and judgment was demanded for the entire indebtedness of 1.2 million dollars. A "second amended complaint" was filed. The plaintiffs sought to join as parties defendant "in a class action under Rule 23 a class to include all known bondholders", sought the sale of the "bond estate", and joined as "specific defendants", Walter Podrog, L. T. Perry, J. W. Caperton, and the Union Planters Bank of Memphis. Most significantly, the plaintiffs sought a declaratory judgment that all actions taken by the Trustee Bank, its agents, servants, employees and attorneys were proper and in the best interests of the Bondholders.

On July 22, 1975, in an uncontroverted hearing, Chancellor Summers signed an order which purported to exonerate the Trustee Bank, and its agents and attorneys, of any liabilities on account of its actions as Trustee. But on September 11, 1975, Chancellor Summers entered a sua sponte order that the approbation accorded to the Trustee was premature and that the matter was too friendly. He vacated the July 22, 1975 order.

Thereafter on November 24, 1975, Chancellor Summers certified the action as a class action and designated Podrog and Manning as Representatives of the Class. Podrog answered pro se on January 9, 1976, and sought plenary affirmative relief based upon generalized assertions of fraud.

On November 24, 1976, the Bondholder Class Representatives formally answered and counterclaimed against the Security Bank and Trust Company, the Town of Grand Junction, and the law firm of Waring, Cox, James, Sklar, and Allen. Later, the law firm of Phipps, Johnson and Holmes, of Ponca City, Oklahoma, was joined as a defendant.

Security Bank and Trust Company by answer generally and specifically denied a breach of fiducial duties, and cross-claimed against the Town. The Town denied liability and cross-claimed against the Trustee Bank. The law firms denied that they had breached any fiducial duty, or that they were negligent. The parties were re-aligned to make the Bondholders plaintiffs and the action sustained as one properly brought on behalf of the Class. All proper notices were served upon the bondholders (about 140) and about 5 of them chose not to participate.

The real and personal property of Fabricating, Inc. was sold by the Clerk and Master. A portion of the funds realized from the sale has been paid to the bondholders, with the balance retained by the Clerk and Master. The bondholders class representatives settled with the Security Bank and Trust Company for $250,000.00, and this settlement was approved by the Court after notice of it was sent to the bondholders, giving them an opportunity to object. None objected, and their class representatives testified in open Court that the settlement should be approved.

II

The Facts

The voting residents of the Town of Grand Junction were the targets of a carefully planned, orchestrated scheme involving the issuance of industrial revenue bonds.

The sordid scheme possibly began in 1972 when Carl Dunn, Jr., (whose father, it will be remembered, was Mayor) a salesman with the boiler room brokerage firm of Investors Associates of America, Inc., of Memphis, prepared this aberration:

> "The principals Charles E. Bruce and E. C. Holman are interested in building a pre-fab factory in Grand Junction, Tennessee, which will be incorporated in Tennessee under the trade style and name Fabricating, Inc. . . .

In addition, the corporation has the ways and means of financing and building an entire new city of approximately forty thousand people. The present plan consists of buying three to four thousand acres of land adjacent to and including parts of Grand Junction, Tennessee, which will be developed into a new modern smokeless city and will be known as the Rebirth of Grand Junction, Tennessee. The main conception would be to start off with a professional eighteen hole golf course, riding and boarding academies for horses, tennis courts, fishing lakes and in general all around recreational facilites in which residential lots will be intermingled in and around various activities. From this point an industrial, office, shopping center, and school area will be initiated.

The theme for the corporation sales of lots will be private schools to eliminate busing, a city built with a minimum of maintenance which can be run and governed by people without the assistance of any government aids, plus the enjoyment of recreational living away from the stress and strain of big city living. It is felt that with the easy commuting distance to Memphis and surrounding areas, plus the large population to draw from the sale of lots will go as fast as they are available. Sales representatives will be located in the various geographical areas to handle the sales for the various projects outlined above as well as selling modular homes and buildings in the areas they represent. The construction and materials for the new proposed city will be handled by the corporation."

The stage was set for the official entrance of Charles E. Bruce and E. C. Holman, self-styled "Texas Millionaires". Bruce was formerly a resident of Hardeman County; he and Holman had previously formed an entrepreneurial, multi-state liason. They initially suggested to the Mayor that the proposed industry would manufacture color television sets but this idea was discarded in favor of the manufacture of modular motel units.

The legal machinery to accomplish the intended purpose was quickly set in motion. Mr. Sklar of the Memphis law firm of Waring, Cox, etc. was employed by the Town as Special or Bond Counsel upon the suggestion of Investors Associates of America. He prepared and obtained a charter for Fabricating, Inc. Bruce and Holman subscribed to all authorized capital stock ($200,000.00) which was never issued or paid for; Investors Associates was declared the Fiscal Agent for the financing of Fabricating, Inc. The Security Bank and Trust Company of Ponca City, Oklahoma, was selected either by Sklar or Investors Associates as Trustee. The decision was made to raise 1.2 million dollars by issuing 1,200 bonds of $1,000.00 denomination.

Principal and interest would be paid semi-annually from rentals received from Fabricating, Inc. by the Trustee. As additional security (the bonds were secured by a first mortgage on the real estate) Bruce and Holman, lavishly and oft-described as "Texas Millionaires" would personally guarantee the payment of all interest and principal. The offering Circular was jointly prepared by Mr. Sklar and the underwriter; the guaranty, Construction Deposit Agreement, and Indenture were prepared by Mr. Sklar.

The Offering Circular dated October 13, 1972, contains these caveats:

> "The information set forth herein has been obtained from the Town, the Company, the Guarantor, and other sources which are believed to be reliable, but it is not guaranteed as to the accuracy or completeness thereof, and is not to be construed as a representation by the underwriters. This info and expressions of opinions of herein are subject to change without notice..."

A
N
D

"Brief descriptions of the...guarantor including their financial statements are included hereafter in this Offering Circular. Such descriptions do not purport to be comprehensive or definite...."

A
N
D

"...The potential customers are not the leaders of their respective industries and the failure to perform by these potential customers could have an adverse effect on Company..."

The personal guaranty of Bruce and Holman was accompanied by financial statements by a purported C.P.A. named Cantu, of Dallas. Reference is made to these financial statements because they triggered this complex litigation. These statements were fraudulent; Cantu, if he existed at all, was the name of a dishwasher in a Dallas restaurant; the Notary Public likewise was a fraud. Bruce and Holman were not "Texas Millionaires"; they were merely con-men. A great deal of proof was offered to justify or alleviate the naivete of those taken in by Bruce and Holman, with special emphasis upon the right of Mr. Sklar to assume the prima facie worth of the financial statements. This fact will be discussed in later detail.

The bond issue was purchased by the Underwriter (Investors Associates) for 80% of par, and subsequently sold to banks in Alabama and South Carolina which had loaned Investors Associates the funds necessary to purchase the issue. (There were two issues, each for $600,000.00, six months apart.)

These Banks peddled the bonds to various purchasers, including other brokerages, in the United States. The net proceeds were delivered to the Trustee Bank pursuant to the Construction Deposit Agreement.

A tract of land owned by the Board of Education of Hardeman County on which was located a school building was acquired for $27,000.00. A contract was awarded for the remodelling of the building and the construction of a pre-fabricated steel building to Bruce and Holman. The steel building was erected by Tenn-Tex Company, owned by Bruce or Holman. Bruce was employed as Engineer for the project.

Mayor Dunn was employed by Bruce and Holman, (Fabricating, Inc.), as Plant Manager at a salary of $1,000.00 monthly. The town Recorder, Byron Black, was also employed.

The too-obvious conflict appearing, the governing body of the Town adopted a Resolution whereby Recorder Black approved all purchase orders and requisitions, but this did not deter Mayor Dunn, who "approved" joint orders with Engineer Bruce, for sums in excess of $300,000.00 to be deposited in the Construction Account of Fabricating, Inc. Dunn paid these funds, and more, to Bruce and Holman, ostensibly for equipment and mahcinery, a substantial portion of which was never delivered. Bruce and Holman, with the connivance, or passive cooperation, or naive approval of Recorder Black and Mayor Dunn, defrauded and hoodwinked Fabricating, Inc., or more properly, the bondholders, out of $491,000.00.

Fabricating, Inc. functioned just long enough to justify the scheme on a short term. Its production was shipped, by Mayor Dunn, to a Georgia concern owned, believe it or not, by Bruce and Holman, who, quite naturally, neglected to pay the invoices.

A significant side-light involves the Tennessee Pewter Company, Inc. Mayor Dunn, with his brother-in-law Smith, and, once again, Bruce, decided the building would accomodate another "industry". They organized Tennessee Pewter Company, Inc. and both capitalized and financed it by the simple expedient of raiding Fabricating, Inc.'s bank account to the extent of $35,000.00. These funds, of course, were part of the bond

proceeds. [From the Bench the Court ordered that a judicial attachment issue on the property of Tennessee Pewter, Inc.]

Fabricating, Inc. paid no rent to the Trustee Bank and formal default occurred October 1, 1974. Applied pressures resulted in Bruce making a payment of $20,000.00 on the accrued rentals; once the fraud became notorious suit was filed by the Trustee against Bruce and Holman in a Texas Federal Court resulting in the recovery of the relatively small sum mentioned in the settlement agreement.

One of the bondholders, Walter Podrog, did not lightly accept the demise of Fabricating, Inc., and the concomitant worthlessness of the bonds. When he learned that the guaranty of Bruce and Holman was worthless, and always had been, his indignation knew no bounds. He began a campaign of disclosure and criticism of the Town, the Sklar firm, the Johnson firm, and the Trustee Bank. These accusations by Mr. Podrog greatly exercised those targeted; their response, or reaction, was to file the complaint, previously described, seeking judicial exoneration or absolution on account of the matters herein briefly described.

III

Conclusions

Mr. Sklar insists that the statute of limitations, TCA 28-304, bars the action against him and the firm. He points to the fact that default admittedly occurred on October 1, 1974, more than one year preceding the filing of the counter-claim, and that the cause of action accrued on this date. The Court does not agree; *Teeters v. Curry,* 518 S.W.2d 512, interprets the statute to mean the action accrues when the claimant knows, or with dilligence should know, that he has been harmed by the negligent or unlawful acts of another. The date of this knowledge may be imprecise under this record, but Podrog's pleading tolled the statute. Furthermore, the Court is of the opinion that the

preponderance of all the evidence—the burden of proof on the subject aside—supports the bondholders insistences that their knowledge of the actions of Mr. Sklar was gained less than one year prior to their counterclaim.

Mr. Sklar insists that he had no "duty whatever", as he testified, to Bond purchasers. He argues that they did not employ him, that as a matter of fact they did not exist when he was employed by the Town, that there was no reliance upon him, or his representatives, and that he had no scienter, or knowledge, of the fraud. The Court agrees in principle with these arguments, but subject to the exception that if information furnished to Bond Counsel by the Underwriter, or the Town, or anyone else, is false, or known to be false, or suspected to be false, or excitingly irregular, and counsel nevertheless without investigation utilizes the information in the Offering Circular, he would be liable, and ought to be. It must be presumed that purchasers would reiy not merely on opinion of Counsel as to legality of bonds or their tax exempt status - anyone who reads a business newspaper knows this - but would also rely on the integrity of all information appearing over counsel's signature. The principle of liability should include those situations where counsel had no actual notice of fraud [and Sklar had no actual notice; he was duped like all the others] but nevertheless the information furnished was of such nature to excite the suspicions of any reasonably prudent attorney. Here are some of the circumstances which should have messaged Mr. Sklar:

(1) The bond issue was essentially promoted by Investors Associates of America, which, prior to the second issue, was the target of an SEC investigation which accused the principles - Hamilton, et al - of dishonesty. Sklar knew this, but was disdainful because "all brokerage houses are investigated".

(2) C. W. Dunn, Jr., of Investors Associates prepared the silly, hyperbolic "Rebirth of Grand Junction" statement which

was edited by Mr. Sklar. This grandiose scheme, amateurishly presented, superimposed upon the reputation of Investors Associates, should have sounded a warning for Mr. Sklar. Puffing one's services and wares has become commonplace and expected, but artless flights to unreality should be premonitory. Further superimposed was the suggestion that a small bank located 500 miles distant in Oklahoma, should be Trustee. There are several banks in Shelby County, Tennessee, which are authorized to exercise trust powers. Further superimposed was the fact that Investors Associates was receiving $240,000.00 for its underwriting, less expenses of $24,000.00 to Mr. Sklar and some others of relative insignificance. The Court agrees with witness Mitchell of the J. C. Bradford Company, that this discount was utterly unconscionable and should have triggered an inquiry. Mayor Dunn even inquired of the law firm if the amount of this discount could be concealed!

(3) The financial statements of Bruce and Holman, prima facie, should have served to put any prudent person - much less a bond attorney - on notice that all was not well. These statements are amateurishly prepared as to form; the context is irregular; the language is crude and unprofessional. The statements are, as witness Simmons stated, "pathetic". It seems to this Court perfectly plain that any intelligent person who had ever studied a financial statement just one time previously, would have instantly realized that these statements fell far short of professional worth and that Cantu, whose address does not appear on the statements, was not an accountant, much less a C.P.A. Mr. Sklar says that he routinely asked a C.P.A. named Brock, whose office is located in the same building which houses the law firm, to inspect these statements. Brock testified that he did not remember this request, nor did he remember the statements. He further testified, when shown the statements, that it would be difficult to assess their worth because he knew - now - they were fraudulent. [The same hindsight caveat applies to the Court.]

The personal guaranty mentioned prominently in the Offering Circular must be presumed to have importantly influenced the purchase of these bonds. Mr. Sklar should have realized that the financial statements were, at bare minimum, suspicious, and he should have made, at the very least, a cursory investigation. Had he done so, such as a telephone call to the Board of Public Accountants, or some such, in Austin, he would have discovered that Lester Cantu was not a C.P.A. The discovery of this one fact would have revealed the entire fraud.

The Court sees no escape from the conclusion that Mr. Sklar treated this matter too lightly and too negligently, and that his negligence contributed as a proximate cause, if that term may be used, to the losses suffered by these bondholders.

The lack of privity is a troublesome issue - see Taglioferro vs. Koella, E.S., Court of Appeals, 1979 - but the Court concludes that privity, in a legal sense, existed between Bond Counsel and Bond purchasers. Otherwise, the prestigious and inducing opinion of counsel would have little weight and no value. There would really be no need to employ Bond Counsel. Furthermore, counsel knows that the information appearing above his signature will be relied upon by a prospective purchaser. Presumably, the fee of $24,000.00 was payment for something other than the routine copying of documents and a few trips to Grand Junction.

The issue of reliance has previously been discussed, and Mr. Sklar's liability under the Municipal Securities Law of 1972 will be discussed later.

It should be mentioned that before the second issue, the Financial statements of Bruce and Holman were amended. Bruce's alleged net worth was nearly doubled, and in a remarkably brief period. His C.P.A. "Cantu" included about $500,000.00 from the bond sales in Bruce's statement, as owned by Bruce. Mr. Sklar saw this incredible and glaring fraud, and wrote to Mr. Bruce that he ought not to include these trust

funds in his personal statement. At this time, the Trustee Bank still retained more than $500,000.00; had Mr. Sklar notified the Trustee of Bruce's action, the Trustee could have retained the funds in its possession, and averted a substantial portion of the loss to the bondholders. But Mr. Sklar did nothing beyond writing the letter to Bruce. As Mr. Maner, Bond Counsel of Savannah, Georgia, put it, "It is not the duty of Counsel to investigate, but to disclose."

IV

The liability of the Town of Grand Junction will be next considered.

Bruce and Holman appointed Mayor Dunn as Plant Manager before the earth was broken for the building. The town council, aware of conflict, thereupon provided that Recorder Black would, in lieu of the Mayor, approve all requisitions and expenditures. But Bruce and Holman countered this safeguard by employing Black also.

Thus it was that Bruce and Holman covered their tracks, as it were, or eliminated possible discovery, by employing the only two town officials who possibly could pose a threat to them.

But Mayor Dunn nevertheless gained access to the bond proceeds, as heretofore described, and paid the proceeds out in a grand fashion to Bruce and Holman.

All this was in direct, flagrant violation of the Town's own contract - the Construction Deposit Agreement - executed in large measure to protect the Town, but violated by the Town in a most execrable manner.

The Mortgage, Indenture of Trust, and Security Agreement dated October 1, 1972, executed by the Town as Grantor, and the Security Bank and Trust Company, as Trustee, contains this provision:

> "Whereas, to so induce Fabricating, Inc. to expand its manufacturing enterprises, plants and related facilities in the State of Tennessee....."

This provision was a blatant falsity. Fabricating, Inc. was a brand new company; it had no history, no manufacturing enterprises, no plants and no related facilities to expand. Its capital stock of $200,000.00 had never been subscribed (and not to this day) and all concerned knew of these omissions, irregularities, misrepresentations and inanities.

While it may be that the actions of Mayor Dunn and Recorder Black may well have been culpable - as distinguished from merely having been committed negligently or ignorantly -the fact remains that the Town condoned what they did, and what they were doing. Mayor Dunn, after he was put on Fabricating, Inc.'s payroll, told Bruce, whom he had known for many years, "*not to pad your invoices too much*".' Dunn admitted this defalcation and breach of trust. An agent who goes beyond his authority does not bind his principal ordinarily; but, here, the Town government knew exactly what the Mayor and Recorder were doing.

The town is, of course, immune from liability unless the Municipal Securities Law of 1972 controls.

As held in *Crowe v. Hospital, 579 SW2d 888 (1979):*

> "Although municipalities do not fall within the aegis of the sovereign immunity doctrine if they are acting in a proprietary capacity...they are considered arms of the state in the exercise of their governmental functions and, hence, are immune from suit."

The issuance of industrial revenue bonds is a governmental function and the Town is immune from suit unless the Securities Act of 1972 requires a different conclusion.

The act makes it unlawful:

(2) "...for any person, in connection with any transaction or transactions in this state which involve the offer to sell ... municipal securities...either directly or indirectly... to engage in any act, practice, transaction or course of business which operates or would operate as a fraud or deceit upon the purchaser...."

TCA 9-1402(q)(2)

The Act provides (TCA 9-1402(f)) that 'fraud', 'deceit' and 'defraud' are not limited to common law deceit; that 'person' (I) means a corporation, a government, or a political subdivision of a government; that municipal security (1) means any bond issued by any town. It is further provided that (TCA 9-1421(a)) any person who violates TCA 9-1402 (g) (2) (b):

"Shall be liable to the person purchasing the...security for any loss incurred...."

Both Mr. Sklar and the Town argue that, like certain SEC regulations, scienter is required, and must be proved, to establish a violation of the act.

The Court does not agree.

The legislative intent is clear: Whoever practices fraud and deceit upon a bond purchaser is liable to the purchaser. The rigorous proof required to establish common law deceit is not mandated; the act does *not* provide "Whoever *knowingly* practices fraud and deceit"; it means what is says and the legislative intent (to correct the unsavory boiler room bond sales in Tennessee, particularly in Memphis) must be effectuated. It is not believed, therefore, that scienter is a necessary element. All that is required is a truthful showing that fraud and deceit were practiced.

The Act applies with greater force to the Town of Grand Junction than to Mr. Sklar. The latter merely was negligent in failing to heed a dozen signals of peril, while the Town merely winked at the antics of its Mayor.

The Court does not look upon this fiasco lightly. While a purchaser of non-rated, industrial revenue bonds, of a small, undercapitalized plant with no history, no experience, and no customers, must assume a correlative risk, he may also assume that he is not being defrauded. As stated in 64 CJS, Municipal Corporations, page 602,

> "By the great weight of authority...if the municipality through its officers or agents is guilty of negligence...it is directly liable to the bondholders for the losses or damages thereby sustained..."

The Court concludes that by the enactment of the Municipal Securities Act of 1972, the General Assembly of Tennessee expressly waived the governmental immunity of political subdivisions which issue municipal securities. Any other conclusion would rather obviously emasculate the Act.

A final point requires some discussion. TCA 6-1709 provides that no holder of revenue bonds shall have the right to compel the exercise of taxing power of the municipality to pay the bonds or interest thereon.

The Court agrees with the bondholders that this statute bars an action on the bonds, but that it does not bar an action based upon a violation by the Town of the Securities Law. Again, to hold otherwise would emasculate the Securities Law. Because of the frenetic efforts of many towns, of which Grand Junction is a prototype, to secure industry, and the avid, and usually uninformed but overwhelming voter approval of any revenue bond issue, the Securities Act is a most salutary piece of legislation, and it should be rigorously enforced.

V

The Court therefore concludes that Mr. Sklar and his law firm as constituted in 1972 are liable to the extent hereinafter indicated; that the Town is also liable to the extent indicated.

The Security Bank and Trust Company settled its Liability and the settlement was approved. The Court does not consider the fault of the Trustee Bank to be any more egregious than that of Mr. Sklar or the Town; their actions were intertwined, interlocking, dependent on each other, and equally tainted. It was ruled from the Bench that the Trustee's cross-claim against the Town was dismissed; similarly, the Town's cross-claim against the Trustee is dismissed. The Johnson law firm was dismissed from this litigation solely because there was no evidence offered to onerate them, excepting some letters written by Mr. Johnson as a defense to the Podrog attack. The dismissal of the cross-claim against the Town, and the dismissal of the complaint against the Johnson law firm, are here reaffirmed.

It is not seriously disputed that, in round numbers, $491,000.00 was lost to Bruce and Holman. The recovery will be limited to this amount because, even absent fraud, and with all good faith and best efforts, the plant may weil have failed and imperilled the purchasers of bonds who financed it. Therefore, they must absorb part of the loss as part of the risk. Interest from February 25, 1976, at 8% is allowed.

Counsel for the bondholders will prepare judgment accordingly. An appeal being presumed, the Clerk and Master should take care *not* to include unnecessary matters, papers, depositions, interrogatories, motions, responses, letters, etc., in the transcript this causes the Appellate Court to become exercised. If in doubt, consult with the Clerk in Jackson. The question of fees and expenses is reserved.

It was brought to the attention of the Court that Mayor Dunn, following default, purchased 15 bonds at an 85% discount.

This absolutely will not be tolerated. He is declared not to be a member of the class, and is excluded.

/s/William H. Inman
Designated Chancellor

APPENDIX D

IN THE COURT OF APPEALS OF TENNESSEE
WESTERN SECTION AT JACKSON

(Hardeman Equity)

Security Bank & Trust Co. of
Ponca City, Oklahoma, and
The Town of Grand Junction,
Tennessee,
Plaintiffs,

vs.

Fabricating, Inc., et al.
and J. Frank Manning and
Walter Podrog, Rep. of
Class of Bondholder of Town
of Grand Junction Bonds Dated
10-1-72,
Defendants and
Counter Claimants,

vs.

The Above Named Plaintiffs and
Waring, Cox, James, Sklar &
Allen and Phipps, Johnson &
Holmes, Kent C. Phipps, Charles
A. Johnson and Kenneth E. Holmes,
Law Firm,
Counter Defendants.

(Honorable William H. Inman,
Chancellor by Appointment)

Leo Bearman, Jr., of Memphis for the Sklar firm, Heiskell, Donelson, Bearman, Adams, Williams & Kirsch of counsel.

Dale Woodall and Ernest G. Kelly, Jr., Cobb, Edwards, Nichol, Woodall & Kelly of Memphis for the Town of Grand Junction.

H. Morris Denton, Denton and Cary of Bolivar, and Agnes Thornton Bird and Frank B. Bird, Bird, Navratil & Bird of Maryville for the Bondholder Class.

AFFIRMED IN PART, REVERSED IN PART, REMANDED

Opinion filed: Feb. 3, 1981

MATHERNE, J.

This lawsuit involves alleged illegal acts in the issuance of $1,200,000 Town of Grand Junction, Tennessee, First Mortgage Revenue Bonds and the improper handling of a trust fund set up from the proceeds of the sale of the bonds. The issues presented on appeal can best be explained by a statement of the position of the parties, the pleadings and judgment in the trial court.

I. The Position of the Parties

The Town of Grand Junction, Tennessee (Town) is a municipality vested with the power and authority to issue revenue bonds as authorized under the Tennessee Industrial Building Revenue Bond Act of 1951, T.C.A. §§ 7-37-101 through 7-37-116. The general plan of that chapter is to permit the issuance of bonds for the purpose of obtaining funds for the construction or extension of manufacturing facilities. The bonds are not general obligation bonds, but are to be retired, principal and interest, from rentals charged to an industry which leases the facility. The lease, the physical plant and equipment are encumbered as security for the payment of the bonds. In many cases, as in the present situation, the bonds are further secured by the personal guaranty of individuals who own the lessee corporation.

Charles E. Bruce and E. C. Holman are self proclaimed "Texas Millionaires" who claimed to be interested in constructing an industrial plant in the Town for the purpose of manufacturing modular motel units. Bruce grew up in the Town and was known and generally respected by the local people. These in-

dividuals contacted the mayor of the Town, Carl Dunn, Sr., concerning the issuance of revenue bonds for the purpose of constructing and equiping the facility which was to be leased to and operated by Fabricating, Inc., a corporation owned by Bruce and Holman. The bond issue was to be personally guaranteed by Bruce and Holman.

Financial statements of Bruce and Holman were submitted as having been prepared by Lester H. Centu, C.P.A., of Texas. These statements of the guarantors were included in the Offering Circular which described to prospective purchasers the entire bond transaction.

Investors Associates of America, Inc., of Memphis, Tennessee, was at that time in the business of underwriting the issuance of municipal bonds. This concern had experienced some difficulty in the past concerning its underwriting endeavors and was described by the chancellor as a "boiler room brokerage firm." The principals of Investor's Associates were Clarence Hamilton, Jerry Hamilton and William (Bill) Harper. a salesman for Investor's Associates was Carl Dunn, Jr., the son of the mayor of the Town. Apparently, through the efforts of Carl Dunn, Jr., Investor's Associates was engaged as the underwriters for the bond issue.

Jerald Harris Sklar, attorney and partner in the law firm of Waring, Cox, James, Sklar and Allen of Memphis, Tennessee, (the Sklar firm) was employed as bond counsel in the issuance of the bonds.

The Security Bank and Trust Company of Ponca City Oklahoma, (Trustee Bank) was designated as the trustee to receive the proceeds from the bond sale and to administer that fund in accordance with the terms of the lease to Fabricating, Inc., an Indenture of Trust and a Construction Deposit Agreement.

The bonds were sold at a 20% discount in two issues, one issue was purchased by a bank in Alabama and the other by a

bank in South Carolina, which banks promptly resold the bonds ($1,000 denomination) to various individuals and concerns over America. The sale proceeds were deposited with the Trustee Bank; and Fabricating, Inc., Bruce and Holman proceeded with the construction of the facilities in the Town.

It appears that Fabricating, Inc., was the general contractor to construct the facility. Bruce was on the job directing this endeavor and he was named as the party to approve payments to Fabricating, Inc., as the construction progressed. Fabricating, Inc., hired Mayor Dunn to oversee the construction, at which time the Town appointed its recorder, Byron Black, as the person to approve payments for the Town as construction progressed. Bruce also arranged for the purchase of all materials and equipment through firms he controlled. It thus developed that Bruce was the lessee, the contractor, the seller, the buyer and one approving agent for materials and equipment for the project. These facts were known to the Trustee bank. It further appears that much equipment was billed to the project at inflated prices and that the trust fund was wrongfully depleted of several thousand dollars.

When the October 1, 1974 payment on the bonds fell due, the lessee, Fabricating, Inc., defaulted and Bruce and Holman failed to make good their guaranty. That happening caused a flury of excitement and what appears to have been the first investigation of Fabricating, Inc., Bruce and Holman. It developed that at the time the bonds were issued Fabricating, Inc., had paid-in capital of less than $1,000; Bruce and Holman were not "Texas Millionaires" but were more accurately described by the chancellor as "con-men;" if Lester H. Centu existed at all, he was a "dishwasher at a restaurant in Dallas, Texas," and most certainly not a C.P.A.; and various irregularities appeared in the manner in which the Trustee Bank handled the trust funds. These developments and the consequential "fixing of the blame" resulted in the present litigation.

II. The Pleadings and Judgment

Upon default, the Trustee Bank filed a lawsuit in a federal district court in Texas against Bruce and Holman on their guaranty. That lawsuit resulted in a judgment against the defendants, in the amount of $1,488,000, but, as will be hereinafter noted, any further amount realized from that judgment is not now available to the bondholders.

On February 10, 1975, the Trustee Bank and the Town filed the present lawsuit in the Chancery Court sitting in Hardeman County, Tennessee, against Fabricating, Inc., Bruce and Holman to recover past due and unpaid rentals of about $59,000 and for the appointment of a receiver to take over the project. The Trustee Bank hired the Sklar firm, the original bonding attorneys, as lead counsel and it was also represented by its general counsel, Charles Johnson, of the firm of Phipps, Johnson & Holmes of Ponca City, Oklahoma. At that time the Town was represented by E. J. Harris, attorney, of Bolivar, Tennessee. Chancellor Summers appointed Carl W. Dunn, Sr., Mayor of the Town, as receiver under a $1,000 bond. Fabricating, Inc. was permitted to continue its operations, but all net revenues were to be paid over to the receiver.

On April 22, 1975, the complainants filed an Amended Complaint wherein they alleged that Fabricating, Inc. was shipping manufactured goods to concerns in Texas and Georgia owned by Charles E. Bruce. The complainants further alleged that these goods had not been paid for and were carried as accounts receivable on Fabricatings' records. It is also alleged that this practice resulted in a misappropriation of the assets of Fabricating, Inc., to the detriment of the bondholders for whom the Trustee was acting. The complainants prayed for money judgment in the amount of $1,200,000 plus interest accrued on the bonds, and requested the appointment of a reveiver to take over the full operation of Fabricating, Inc. A hearing was had on the prayers of the Amended Complaint, and

by decree entered on July 22, 1975, Chancellor Summers found certain facts and ordered a reference to the clerk and master to examine weekly the operations of Fabricating, Inc. and to report to the court. This decree also found that "the acts of the Trustee to date in this matter are hereby approved and confirmed as being reasonable and prudent acts under the circumstances."

On August 18, 1975, the defendants filed their joint answer to the complaint.

On September 13, 1975, Chancellor Summers, of his own motion, filed an Interlocutory Opinion and Order wherein he overruled his prior opinion which absolved the Trustee and gave the parties 30 days therefrom in which to supply the court with certain information so that the court could get a clear picture of the entire situation.

On October 20, 1975, the complainants filed a motion to be allowed to file their Second Amended Complaint. By that pleading the complainants asked that all bondholders be made parties defendant as a class; that the assets held in trust be sold and applied to the retirement of the bond indebtedness; that the court render a declaratory judgment that all actions taken by the Trustee "its agents, employees and attorneys" in administering the trust be approved as having been in the best interests of the bondholders; that the court find that the Trustee, its agents, employees and attorneys, had not in any way breached its fiduciary relationship to the bondholders in the administration of the trust; and for general relief. By Order filed on November 24, 1975, Chancellor Summers granted the motion to file the Second Amended Complaint; declared the bondholder as a class to be parties defendant; directed that proper notice be given to each member of the class; and named Walter Podrog, L. J. Perry, J. W. Caperton and Union Planters National Bank as class representatives. The Second Amended Complaint was filed on November 24, 1975.

J. Frank Manning, a holder of $25,000 of the bonds filed his Separate Answer generally submitting his rights to the court. On January 9, 1976, Walter Podrog filed his Answer, *pro se*, alleging that the Trustee Bank, its officers, agents and attorneys administered the trust fund in a negligent, careless and improper fashion; that the bondholder's losses will be "primarily due to the fraudulent financial statements of guarantors, that were permitted by the Trustee and all others involved in the promotion and sale of the bonds, to be published and circulated to prospective bond purchasers . . .;" and for general relief.

By order dated February 25, 1976, Frank Bird and Agnes Bird were recognized as attorneys for the defendant class and were authorized and directed to "personally audit the litigation presently being carried on in the Federal Court in Texas, involving the Trustee and the individual Guarantors for Fabricating, Inc."

Thereafter, by orders of the court, all assets of Fabricating, Inc., were sold.

On November 24, 1976, the Bondholder Class Representatives filed an Answer and Counterclaim. By answer they denied that the Trustee Bank, its agents and attorneys, had properly administered the trust fund. By counterclaim they aver specific acts and failures to act on the part of the Trustee Bank which constitute gross and unexcusable negligence in the performance of its fiduciary duties, all to the detriment of the bondholders. Also, by counterclaim, those parties aver that the Sklar firm, as bonding attorneys in the issuance of the bonds, failed to fully and faithfully discharge their duties to the bondholders, alleging specific acts of misfeasances and nonfeasances all to the detriment of the bondholders. The counterclaim acknowledged that the Sklar firm may have already made itself a party to the lawsuit, but to avoid any doubt, prayed process issue against it. The counter-complainants sought damages in excess of $1,000,000.

By amendments to the counterclaim, the bondholders aver that the Trustee Bank, the Town and the Sklar firm violated the provisions of the Tennessee Municipal Securities Act of 1972, and particularly T.C.A. § 9-1402(g) thereof in the issuance of the bonds; that the Sklar law firm and the Johnson firm had concealed and failed to disclose material facts relative to the rightful claims of the bondholders against the Trustee Bank and that the true facts were neither discovered by the bondholders nor subject to such discovery until March 24, 1976; the Johnson firm was made a party defendant; and specifically stated certain violations by the Trustee Bank of its obligations under the Construction Fund Account (an account set up for the construction of the project from funds received from the sale of the bonds).

Many additional pleadings, motions, counterclaims and cross-claims were filed but need not be here considered. Under the pleadings the lawsuit developed into one in which the real plaintiffs were the bondholder class and the defendants were the Town, the Trustee Bank, the Sklar firm, and the Johnson firm. In the meantime Chancellor Summers had left the chancery bench and the Supreme Court of Tennessee appointed Chancellor William H. Inman to hear the lawsuit.

The bondholder class took a voluntary non-suit as to Bruce and Holman. Chancellor Inman dismissed the Johnson firm. The Trustee Bank settled by the payment of $250,000 into court, and was assigned all amounts it might collect on the Texas judgment against Bruce and Holman. Judgment in the amount of $1,488,000 was entered in favor of the bondholders against Fabricating, Inc. There is no appeal from any of the foregoing judgments.

After a full hearing, Chancellor Inman held that the Town and the Sklar firm had violated the Tennessee Municipal Securities Act of 1972, and entered judgment against them in the amount of $391,611.38, holding that the court was not willing to recompense the bondholders *in toto*, but would restrict

the recovery to what the court found to be the direct loss. The judgment was to bear interest at 8% per annum from February 25, 1976, which resulted in a judgment of $505,768.28. All other claims and cross-claims were dismissed.

III. The Issues on Appeal

The Town, the Sklar firm and the bondholder class each appeal to this court.

The Town argues that it can not be held liable on the bonds because the act under which the issue was made, the Tennessee Industrial Building Revenue Bond Act of 1951, T.C.A. §§ 7-37-101 through 7-37-116, specifically states that the issuing municipality is not to be held liable therefor; it should be allowed recovery over against the Trustee Bank; it is not liable under the Tennessee Municipal Securities Act of 1972; and the chancellor erred in not reducing the judgment by the amount of $250,000 as paid in by its alleged joint tortfeasor, the Trustee Bank.

The Sklar firm insists that: (1) the action against it is barred by the statute of limitations, T.C.A. § 28-304, as relates to actions against attorneys for malpractice; (2) if the attorney-client relationship does not exist between the Sklar firm and the bondholders, the attorney owes no duty to the bondholder; (3) the evidence preponderates against the findings of the chancellor; (4) each bondholder must prove reliance upon the alleged negligence of the attorneys; (5) under the Tennessee Municipal Securities Act of 1972, the bondholders must prove *scienter* in order to prevail; and (6) proper credits have not been given against the judgment rendered.

The bondholder class argues that Chancellor Inman was correct in his rulings on the above issues of the other appellants, and states as an additional issue that the chancellor erred in failing to give judgment for 100% of the amount paid for the bonds, plus interest as accrued thereon, less all amounts paid and available to be paid on the bonds.

In our consideration of these issues it is necessary to first determine the scope of the Tennessee Municipal Securities Act of 1972, T.C.A. § 9-1401, et seq. This act was repealed by Chapter 506 of the Acts of 1976, but it was in full force and effect during the time the transactions being considered were undertaken.

IV. The Tennessee Municipal Securities Act of 1972, T.C.A. § 9-1401, et seq.

The act defines prohibited practices at T.C.A. § 9-1402(g), (1) or (2), as follows:

> (g) "Prohibited practices." The following shall be prohibited practices and shall be unlawful under the terms of this chapter.
>
> (1) For any person knowingly to subscribe to, or make or cause to be made, any material false statement or representation in any application, financial statement or other document or statement required to be filed under any provision of this chapter; or
>
> (2) For any person, in connection with any transaction or transactions in this state which involve any offer to sell or to buy municipal securities, or any sale or purchase of municipal securities, or advising municipalities with regard to financing municipal projects, either directly or indirectly, (a) to employ any device, scheme or artifice to defraud, or (b) to engage in any act, practice, transaction or course of business which operates or would operate as a fraud or deceit upon the purchaser or seller, or the municipality.

We hold that section 9-1402(g)(1) only relates to the requirements of chapter 14 and not to other transactions accomplished in the actual issuance of municipal bonds. The chancellor found a violation of section 9-1402(g)(2), and we must determine the scope of that section as relates to the acts of the Town and the Sklar firm.

We hold that section 9-1402(g)(2) does not relate to or govern the disbursement of funds realized from the sale of municipal securities. That conclusion is required in that the quoted section plainly and expressly refers to "any transaction or transactions in this state which involve *any offer to sell or to buy* municipal securities" (Emphasis added). That section further refers to "*any sale or purchase* of municipal securities," and also to any "advising municipalities *with regard to financing municipal projects,* either directly or indirectly" (Emphasis added).

From the verbiage of the quoted section of the act we conclude that the statute only applies to and prohibits those acts described in 9-1402(g)(2), (a) or (b) when the "person" acting is engaged in (1) the sale or purchase, or the offering of sale or purchase, of municipal securities, or (2) advising municipalities with regard to financing municipal projects. If the "person" charged under the act was not engaged in those activities, that "person" is not liable under the provisions thereof.

This conclusion is further buttressed by other provisions of the act which define terms, require licenses and impose duties on those subject thereto. Note the definition of "broken-dealer" at section 9-1402(e) and "agent" at section 9-1402(d) wherein the words "in effecting [or attempting to effect purchases and sales of] transactions in municipal securities" are used.

We, therefore, hold that for the Town or the Sklar firm to be liable under that statute they must be found to have acted illegally as herein indicated and not in the administration of the trust fund which was realized from the sale of the bonds.

V. **The Sklar Firm**

We hold that the counterclaim of the bondholder class seeking affirmative relief against the Sklar firm based upon common law negligence and the violation of T.C.A. § 9-1402(g) is barred by the one-year statute of limitations as set out at T.C.A. §

28-304. In reaching this decision we have treated the cause of action as having accrued at that time when the bondholders knew or, in the exercise of ordinary care, should have known that they were damaged by the alleged acts of that firm.

The bondholders argue that the statute does not apply because this is an action for declaratory judgment; that the Sklar firm had made itself a party to the lawsuit prior to the filing of the counter complaint which sought affirmative relief against it; and that the Sklar firm concealed from the bondholders the fact that they had a cause of action against it.

As noted in the outline of the pleadings filed, the complaint and the first amendment thereto sought a money judgment for the entire $1,200,000, plus interest, and for the appointment of a receiver to take over the project. The request for a declaratory judgment was in the Second Amended Complaint wherein the Trustee Bank on behalf of itself, its agents, officers and attorneys, sought to be absolved of any liability in the *administration of the trust fund;* it was at this stage that the bondholders were made a party defendant as a class. Making the bondholders defendants at that stage was proper because of the prayer for exoneration of the Trustee bank, its agents, officers and attorneys, from any liability to the bondholders growing out of the administration of the trust fund.

The counterclaim filed by the bondholder class was not limited to issues relative to relief by declaratory judgment. Instead that party defendant sought, for the first time, affirmative relief against the Sklar firm and the Town for all amounts lost by the bondholders as a result of the issuance of the bonds and the handling of the trust fund.

It is important to note that the Sklar firm was not the attorney for the Trustee bank during the alleged illegal disbursements of the trust fund. The Sklar firm was the attorney for that bank only in the bank's effort as trustee to recover from the lessee and the gruarantors the amount due

under the entire bond issue. A declaratory judgment which rendered the Trustee bank, its officers, agents and attorneys, absolved of any liability in the administration of the trust fund would not have affected the Sklar firm one way or the other; it was not before the court as an attorney representing the Trustee Bank *in the administration of the trust fund.*

We have studied the case of *Tennessee Eastman Company v. Adams* (Tenn. 1964) 381 S.W. 2d 269, and conclude that the principals therein enunciated are not applicable to this lawsuit. We have also studied Freeman on Judgments, 5th Ed. § 430, et seq., and conclude that prior to the filing of the counterclaim by the bondholder class the Sklar firm had no interest in the lawsuit which would render it a party thereto.

On the issue of concealment the bondholder class agues that the Sklar firm, in conjunction with the Johnson Firm, conspired to mislead the bondholders as to the existence of their cause of action. If that conspiracy be found, we conclude that it did not mislead the bondholders nor conceal from them their alleged cause of action against the Sklar firm.

By letter dated May 15, 1975, long after he had been appointed as one class representative of the bondholder class, Podrog wrote a letter to the Johnson firm to the effect that "legal action of all types" should be taken immediately; and that "the Town, the Mayor, the Council, Waring, Cox, James etc. Ewing Harris knew or should have known the true character of guarantors, but in their greed, did not check on the financial statements presented by Centu and guarantors, to the serious detriment of the bondholders."

Further, by letter dated July 21, 1975, Podrog wrote the Trustee Bank asking for the names and addresses of all bondholders and made certain request of the Trustee Bank, among which was the following:

> Institute civil suit for damages to all bondholders due to negligence etc. against the Town of Grand Junction, its

Mayor, its Council, Waring, Cox, James, Sklar & Allen, Ewing J. Harris, Hamilton Brothers and Investors Associates of America for failure to verify guarantors' financial statements etc.

Finally, on September 30, 1975, Podrog mailed to all bondholders a letter wherein in the following is stated:

[that he is convinced] that this ill-fated promotion was fraudulently inspired from the start. All involved in the promotion and ultimate sale of Bonds were at least negligent in permitting false financial statements and apparent forged C.P.A. certifications to be publicized and circulated as true.

* * * * * * * *

For almost a year I have requested, demanded and pleaded for a list of the bondholders known to the Trustee, without success. Finally after my submission to Chancellor Paul R. Summers of the Chancery Court many of the above facts, he ordered the Master to send me the list, which was received on September 24th.

* * * * * * * *

The bondholders list supplied me, listed almost 800 of the 1,200 bonds. If these bondholders would contribute 120.00 for each bond owned, the Bondholders Protective Committee would have almost $16,000.00 to retain counsel as well as an investigator to uncover hidden assets of guarantors.

* * * * * * * *

After the total losses to bondholders is determined, civil action for damages should be filed against the Town of Grand Junction, its Mayor, its Council, the original Underwriters and all attorneys involved in the promotion and sale of the Bonds, to the purchasers, due to the

carelessness and negligence in permitting fraudulent financial statements to be published and circulated.

From this September 30, 1975 letter, we must conclude that a court appointed representative of the bondholder class and all known bondholders had notice of their possible claim against the Sklar firm. The bondholder class filed its counterclaim for affirmative relief on November 24, 1976, more than one year from the date that it knew or should have known of its alleged claim against the Sklar firm. The counterclaim is accordingly barred. *Brown v. Hipshire* (Tenn. 1977) 553 S.W. 2d 570.

We are mindful of Chapter 758, Public Acts of 1978, codified at T.C.A. § 28-1-114, effective March 30, 1978, wherein the *Brown v. Hipshire* ruling was legislatively overruled. That statute provides that a counterclaim or a third party complaint is not barred by the applicable statute of limitations if it was not barred at the time the claims asserted in the original complaint were interposed. That statute is not applicable to this lawsuit because the one-year statute of limitations had run in favor of the Sklar firm before the statute was enacted. Basically, where the defense of a statute of limitations is a complete bar to an action, that defense can not be taken away by a subsequent statute. See: *Tennessee Coal, Iron & R.R. Co. v. McDowell* (1897) 100 Tenn. 565, 47 S.W. 153. See also article 1, section 20 of the Constitution of Tennessee which provides: "(t)hat no retrospective law, or law imparing the obligations of contracts, shall be made."

We, therefore, hold that Chancellor Inman erred in rendering judgment against the Sklar firm because the statute of limitations has barred any claim arising out of the issuance of the bonds and there is no proof of negligence or fraud on the part of the Sklar firm in the administration of the trust.

VI. The Town of Grand Junction

Chancellor Inman held that the Town can be held liable only by virtue of the Tennessee Municipal Securities Act, T.C.A. § 9-1401, et seq.

The bonds having been issued under the terms of The Industrial Building Revenue Bond Act of 1951, T.C.A. § 7-37-101, et seq., the Town argues that it is exempt from liability by virtue of section 7-37-109 of that enactment. We agree with Chancellor Inman that the exemption afforded issuing municipalities under The Industrial Building Revenue Bond Act does not afford a municipality immunity from suit under the Tennessee Municipal Securities Act. The Town is a "person" as defined at section 9-1402(i) of the act and may be found liable if guilty of the unauthorized practices set out at section 9-1402(g). We hold that the Tennessee Municipal Securities Act of 1972 was a policing measure which applied to the issuance of all bonds by municipalities whether they be revenue bonds or general obligation bonds.

We also agree with Chancellor Inman that the legislature waived the governmental immunity of a municipality which violated the provision of the Tennessee Municipal Securities Act.

Having held the statute applicable to the Town, we must now determine if the Town violated the provisions of T.C.A. § 9-1402(g) *in the issuance of the bonds.*

We conclude that the record does not establish a violation by the Town of those provisions of the statute. We note that the bondholder class devotes only three and one-fourth pages of a 112 page brief in this court to "The Town's Acts and Omissions in Connection with the Marketing of the Bonds." We further note that the arguments therein presented fail to relate to any direct action by the Town which would establish a violation of the statute. The argument is directed toward the fact that Mayor Dunn and Recorder Black wrongfully relied upon the underwriters and the bond counsel.

Mayor Dunn was 58 years of age at the trial in 1979. He was a retired Lieutenant Colonel in the Army and had no experience or expertise in the field of municipal bonds. Recorder Black was 41 years of age at the time of the trial, a high school

graduate, and was operating a grocery store in Grand Junction at the time the bonds were sold. Recorder Black had no experience or expertise in the field of municipal bonds. If these two officials, totally incompetent in the field of municipal bonds, had not listened to the experts employed to advise them *in the issuance of the bonds,* we could envision possible claims against them for malfeasance in office. We can not accept an argument that they should have acted independently of their expert advice *in the issuance of the bonds.*

Liability of the Town is also sought based upon the fact that Mayor Dunn saw the Cantu financials prior to the closing of the bond issues. That argument infers that Mayor Dunn should have appreciated the alleged falsity of those statements, and he should have sounded the alarm. Mayor Dunn testified that he could not analyze a financial statement, and that he depended upon others involved who apparently were capable of so acting. The bondholder class failed to prove otherwise.

Looking to what the Town did toward the issuance of the bonds we find that the bonds were issued under the provisions of The Industrial Building Revenue Bond Act of 1951. The Town did pass all proper and necessary resolutions pertaining to the issue; it caused a valid and legal referendum to be held on the subject; it pledged the income and revenue to be received from the project to secure the punctual payment of the bonds; it conveyed in trust the real and personal property of the project to secure the payment of the bonds, principal and interest; it filed the necessary papers with the state; it leased the premises for rentals sufficient to retire the bonds as they became due; and it complied with every provision of the statute under which the bonds were issued.

In short, the bondholder class has failed to establish that the Town, *in the issuance of the bonds,* committed any act prohibited by T.C.A. § 9-1402(g). As heretofore noted, that statute does not apply to the administration of trust funds obtained from the sale of the bonds. We, therefore, hold that Chancellor Inman erred in finding the Town liable under T.C.A. § 9-1402(g).

Looking now to the liability of the Town in the administration of the trust fund, we find that the Town in that respect had certain responsibilities. Under the various agreements the Town and the engineer on the job, Bruce, were to approve all expenditures from the trust fund for constructing and equipping the projects.

Mayor Dunn was hired by Bruce to "oversee" the construction and operation of the project. The Town, thereupon, appointed Recorder Black as the person to approve these payments.

As relates to the administration of the trust fund, the bondholder class by its Counterclaim alleges that the Town is liable because (1) its duly constituted officials, Dunn and Black, were negligent and derelict in the performance of their duties in administering the trust fund, and (2) the mayor and recorder, Dunn and Black, became employees of Fabricating, Inc. and Bruce, abandoned their responsibilities as representatives of the Town in the administration of the trust fund, and became the willing tools of Bruce, all to the detriment of the bondholders.

Considering first the charge of negligence on the part of Dunn and Black, we note that on the issue of the administration of the trust fund the Town retained whatever governmental immunity which it otherwise possessed. Some of the alleged negligent acts in approving payments on behalf of the Town occurred before, and some after, the enactment of the Tennessee Governmental Tort Liability Act, Chapter 345, Acts of 1973.

Prior to that statute a municipality was not liable for the negligent acts of its officials and employees while carrying out a governmental function. *Scates v. Board of Com'rs. of Union City* (Tenn. 1954) 265 S.W.2d 563. We hold that the function of Recorder Black in the administration of the trust fund was governmental in nature, and the Town can not be held liable for any damage caused by his negligence in so performing prior to the enactment of the Tennessee Governmental Tort Liability Act.

As to the alleged negligence of Black after the statute was passed, we note that the statute, section 29-20-205, exempts from the removal of immunity all acts of negligence of the city's employees where the loss "(a)rises out of the exercise or performance of the failure to exercise or perform a discretionary function, whether or not the discretion is abused." The bondholder class places discretionary duty on Recorder Black. Their claimed loss having resulted from the alleged negligent exercise of that duty, they can not recover from the Town.

Finally, the bondholders argue that the officials, Dunn and Black, became the "willing tools" of Bruce and failed to perform their official duties, all to the detriment of the bondholders. It is true that Dunn worked full time with Fabricating, Inc., and he and Bruce formed Tennessee Pewter Co., which operated in the facilities provided for Fabricating, Inc. It is also true that Black was paid about eight or nine hundred dollars for part-time night work he did for Fabricating, Inc. during the years 1973, 1974 and 1975. Black also worked for Tennessee Pewter Co. Dunn was the part-time mayor; Black was an elected Alderman and appointed recorder, both positions being part-time only. A review of the record fails to establish the charge that these two men, acting for the Town, were the willing tools of Bruce and Holman. Dunn did not participate in the administration of the trust fund on behalf of the Town. Black did so participate, and there is no showing that he intentionally or willfully acted to the detriment of the bondholders. Negligence on his part may be found, but, as hereto fore shown, the Town is not, under the facts, liable for that negligence.

We, therefore, hold that, under the facts, the Town can not be held liable for any loss suffered by the bondholders due to the alleged mismanagement of the trust fund.

VII. Conclusions

Admittedly, the entire plan for the issuance of the bonds and the development of the project was conceived in fraud and grossly mismanaged. However, we note that the bondholders have a judgment against Fabricating, Inc., and its assets have been sold in partial satisfaction of that judgment; they had a judgment against Bruce and Holman, but the benefits thereunder, if any, were surrendered to the Trustee bank for the payment by that party of $250,000; they had the trustee bank duly before the court for a holding on the misappropriation of trust funds, but chose to release that fiduciary; they did not appeal the order dismissing the Johnson firm relative to the disbursement of trust funds; they did not sue Investor's Associates of America nor Mayor Dunn, individually, and now attempt to fix all blame on the Sklar firm and the Town.

For the reason heretofore stated, we hold that, under the facts, those two parties are not liable. All other holdings by Chancellor Inman are affirmed. This cause is remanded to the trial court for such action as is necessary to fix cost, attorney fees if proper, disburse the funds held for the benefit of the bondholders and enter a final decree which will include the dismissal of the Sklar firm and the Town.

The costs in the trial court and in this court are adjudged against the bondholder class and the clerk and master is ordered to pay such costs from the funds held by him for the bondholders.

MATHERNE, J.

NEARN, J. (Concurs)

HIGHERS, SPEC. J. (Concurs)

APPENDIX E

IN THE SUPREME COURT OF TENNESSEE
AT JACKSON

(Hardeman Equity)

Security Bank & Trust
Company of Ponca City,
Oklahoma, and the Town
of Grand Junction, Tennessee,
Plaintiffs,

v.

Fabricating, Inc., E. C.
Holman and Charles E. Bruce,

and

Walter Podrog, L. J. Perry
J. W. Caperton, Union Planters
National Bank, and All Known
Bondholders of Town of Grand
Junction Bonds Date October 1,
1972,
Defendants.

and

J. Frank Manning and Walter
Podrog, Representatives of
the Class of Bondholders of
Town of Grand Junction Bonds,
Dated October 1, 1972
(Fabricating, Inc.).
Counter-Plaintiffs-
Appellants,

v.

The Above Named Plaintiffs
and Waring, Cox, James, Sklar

and Allen, a Partnership
Composed of Allen LCox, Jr.,
Roane Waring, Jr., Erich
William James, Robert Lee
Cox, Jerald H. Sklar, Lewis
F. Allen and Roger D. Fish,
as General Partner,
Counter-Defendants-
Appellees.

Affirmed Judgment of the
Court of Appeals

JUDGMENT

This cause coming on to be heard upon the record from the Court of Appeals, Western Section at Jackson, application for permission to appeal having been heretofore granted, briefs and arguments of counsel; upon consideration whereof, this Court is of opinion that the judgment of the Court of Appeals should be affirmed for the reasons set out in the opinion filed (a copy of which is attached hereto).

IT IS, THEREFORE, ORDERED AND ADJUDGED that the judgment of the Court of Appeals is affirmed and the cause is remanded to the Chancery Court of Hardeman County for further proceedings not inconsistent with the Court's opinion, and for the collection of the costs of the Court below; for all of which let mandate issue.

Costs incurred in this Court are taxed against appellants-bondholders.

12/19/83.

APPENDIX F

IN THE SUPREME COURT OF TENNESSEE
AT JACKSON, TENNESSEE

(Hardeman Equity)

Security Bank and Trust Co., et al

vs.

Fabricating, Inc., et al.

vs.

The Above Named Plaintiffs,
Waring, Cox, James, Sklar & Allen
et al.

NOTE: In the present posture of this case, the Bondholder Class is the Appellant; the law firm of Waring, Cox, James, Sklar & Allen is the Appellee. (The Town of Grand Junction is not treated as an Appellee in this Brief.)

SUPPLEMENTARY ARGUMENT ON BEHALF OF THE BONDHOLDER CLASS BASED ON THE JUNE 6, 1983 OPINION IN *PICKETT V. BROWN*, 76 L. Ed. 2d 372

Subsequent to the argument of this case before this Court on April 6, 1982, the U.S. Supreme Court has decided a case which bears directly on the sole issue on which this Court requested briefs - namely the statute of limitations issue. Since this Court still has the case under consideration, we believe it proper - indeed required of us as advocates - to supplement our prior arguments on this point by reference to this very recent U.S. Supreme Court case.

The case to which we refer is *Pickett v. Brown*, decided June 6, 1983, and reported in 76 L. Ed. 2d 372; a copy of the Opinion is attached hereto as a convenience for the Court.

Pickett invalidated a Tennessee statute of limitations (TCA 36-224 (2) (1977) on the ground that it violated the Equal Protection Clause of the Fourteenth Amendment. The statute so invalidated limited the time within which illegitimate children may bring an action for paternal support to a shorter period than that for a similar action by legitimate children. The Court held that such a distinction or classification is constitutionally impermissible because of said Equal Protection Clause.

The analogy to the case at bar is clear and compelling.

The effect of the Court of Appeals ruling in the case at bar is to limit the time within which an action must be brought against an attorney for the violation of a statute to a shorter period than that within which a similar action must be brought against a non-attorney—even though the wrongful acts of the attorney and the non-attorney are identical.

In the case at bar the trial judge (Chancellor Inman) found that Attorney Sklar was professionally negligent. He also found that his acts relating to the drafting, publishing and distributing of the Offering Circular constituted a violation of the Tennessee Municipal Securities Act of 1972. (He further found that the Class's action was begun January 9, 1976—not November 24, 1976, which was the date of the filing of the pleading making the detailed charges of wrongful conduct. He also concluded that in any event the Class's "discovery" of Mr. Sklar's actions occurred less than one year prior to November 24, 1976.)

The Court of Appeals without indicating any disagreement with the Chancellor's finding that Mr. Sklar had violated said Act, dismissed the entire suit on the basis of the one year attorney malpractice statute (TCA 28-304).

The effect of this dismissal is, of course, to hold that notwithstanding the fact that a non-attorney may be sued for a violation of the Tennessee Municipal Securities Act for a period of three years (after May 28, 1975—two years—see *Vance v.*

Schulder (Tenn. 1977) 547 SW2d 927 at 931, footnote 2), an attorney for an identical violation may be sued for a period of only one year.

Conceivably, such a holding might pass constitutional muster if the factual situation were such that the attorney's wrongful conduct constituted "the practice of law". That, of course, is not the situation here; here under Chancellor Inman's findings of fact, Mr. Sklar's violations of the Act included his participation, publication, and distribution of the fraudulent Offering Circular (which omitted material facts, and included totally fraudulent financial statements). Such "work", under all the proof, is not "attorney work"—rather it is "underwriter's work". (Even Mr. Sklar's partner, Robert L. Cox, testified that the drafting of Offering Circulars (other than the description of the legal documents) by bond counsel would be ". . . something gratuitous".) (Tr. 611)

Pickett, we submit, is clear and compelling authority that to interpret the attorney malpractice statute of limitation as did the Court of Appeals causes it to run afoul of the Equal Protection Clause, and supports our argument on this point found in our Principal Brief, beginning at page 22 thereof.

We earnestly urge this Court to rule that the Bondholder Class's claims against Mr. Sklar, et al, are not time-barred, and thus avoid an inevitable collision with the Equal Protection Clause as most recently interpreted by the U.S. Supreme Court in *Pickett.*

Respectfully submitted,

/s/ Frank B. Bird
/s/ Agnes Thornton Bird
/s/ H. Morris Denton

Attorneys for The Bondholder Class

APPENDIX G

IN THE SUPREME COURT OF TENNESSEE
AT NASHVILLE

For Publication

March 14, 1977

Trousdale Equity

Honorable Edward M. Turner
Chancellor

Woodson H. Vance,
Petitioner

vs.

Emanuel Schulder, Paul
Schulder, Monroe Schulder,
Victor Reichenstein, and
David Pollack,
Respondents

(reported at 547 S.W.2d 927)

For Petitioner:

Robert H. Goodall
Gallatin, Tennessee

James Donoho
Hartsville, Tennessee

Arthur E. McClellan
Gallatin, Tennessee

For Amicus Curiae
Lloyd E. Clarke:

James M. Manire
Memphis, Tennessee

For Respondents:

Herbert R. Rich
Nashville, Tennessee

For Amicus Curiae
Kemmons Wilson, Wallace E.
Johnson and Harris, Kern
Forster & Company:

George E. Morrow
Martin, Tate, Morrow & Marston
Memphis, Tennessee

James W. McDonnell, Jr.
Canada, Russell & Turner
Memphis, Tennessee

William W. Dunlap, Jr.
Memphis, Tennessee

Marion S. Boyd, Jr.
Canada, Russell & Turner
Memphis, Tennessee

Susan Callison
Canada, Russell & Turner
Memphis, Tennessee

OPINION

AFFIRMED WM. H. D. FONES, J.

The principal issue in this Court is the appropriate statute of limitations applicable to a suit based upon alleged fraudulent representations said to have induced the sale of stock for less than its value.

The five (5) individual defendants were the directors of Hartsville Manufacturing Corporation and of Consolidated Merchandising Corporation. Defendants owned substantially all of the stock of Consolidated Merchandising Corporation and ninety (90%) percent of the stock of Hartsville. Plaintiff, Woodson Vance, owned ten (10%) percent of the stock of Hartsville. Plaintiff filed suit June 23, 1972, alleging that one of defendants, Paul Schulder, "falsely and fraudulently and with intent to deceive and defraud plaintiff" represented on June 18, 1968, that U. S. Industries Inc. had offered to purchase Hartsville for $360,000; that said representation was false and known by all of defendants to be false; that in fact U. S. Industries had offered the defendants $708,000 for all of the stock of Hartsville; that plaintiff was induced to sell his ten (10%) percent interest in Hartsville for $36,000 and that by reason of defendants' misrepresentation he suffered damages in the amount of $34,800.

Defendants denied that any false representation was made and asserted that in fact no separate sum for Hartsville stock

was offered or paid by U. S. Industries; that the complaint showed upon its face that it was barred by the statute of limitations, and other defenses.

The material evidence adduced at the trial was as follows:

Hartsville was originally a cabinet shop in which plaintiff was a one-third partner. In 1959 defendants, or a wholly owned corporation of which they were directors and stock holders, bought fifty (50%) percent of Hartsville and later purchased an additional forty (40%) percent with plaintiff retaining ten (10%) percent. Plaintiff was the plant manager and was paid a weekly salary and received an annual bonus of three (3%) percent of the profits before taxes. His contacts with defendants and the parent corporation owned by them were limited almost entirely to Paul Schulder who came to Hartsville frequently and plaintiff was in touch with him on the phone almost daily. The corporate books were kept in New York but he received annual statements and balance sheets from the company. He acknowledged that he could read a financial statement. He testified that Paul Schulder came to Hartsville on June 18, 1968, and told him that the parent corporation, Consolidated Merchandising, had a chance to sell all of the stock of Hartsville; that in order to do so they needed his stock; that they were going to sell to U.S. Industries for $360,000. Plaintiff agreed and executed a ninety (90) day option to sell his stock in Hartsville to defendant for $12,000 cash, $12,000 in sixty (60) days after the exercise of the option and the balance ninety (90) days thereafter. The option was exercised on July 16, 1968.

It was also part of the agreement that plaintiff would continue as plant manager after the sale to U. S. Industries. Plaintiff testified that in February, 1972, he learned for the first time that U. S. Industries had paid approximately twice the figure of $360,000 for the stock of Hartsville.

Phillip Holder, a certified public accountant testified for the plaintiff. He had no personal knowledge of the negotiations

but he had examined the agreement and plan of reorganization between U. S. Industries and Consolidated Merchandising Corporation and the balance sheets and earnings statements of the selling corporation and its six (6) subsidiaries for the purpose of giving his opinion of the value that U. S. Industries might have placed upon the Hartsville stock in arriving at the total sum paid for the seven (7) corporations. The only figure appearing on the face of the sale agreement was the total selling price paid at the time of closing, June 25, 1968, which was $4,867,000. This sum was to be paid by issuing its equivalent in value of U. S. Industries common stock at its closing price on the New York Stock exchange on said date. The agreement provided that U.S. Industries would issue and deliver to Consolidated Merchandising additional shares for each of the calendar years 1968 through 1972 wherein pre-tax profits exceeded specified amounts. In accordance with the formula specified in the contract additional shares having a value of $1,926,232 were received by Consolidated in 1969 and $1,428,717 in 1970. No additional shares were due in 1971 or 1972 and thus the total sum received for the seven (7) corporations, paid in shares of stock of U. S. Industries, was $8,221,949. The witness Holder compared Hartville's book value and performance with that of the Consolidated group, using four different methods of accounting with produced values ranging from $582,837 to $762,218.[1] He conceeded that these figures did not give any consideration to intangibles, such as good will, trade names owned by corporations in the group other than Hartsville, nor to any advantages or disadvantages of the sale of seven (7) corporations in one package.

Defendant paul Schulder denied telling plaintiff that the company would be sold for a specified sum. He said that the book value of Hartsville at the time of sale was approximately

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[1] These methods were, book value, after tax profits, selling price times book value and multiple of after tax earnings.

$230,000 but the Board of Directors decided that for the purpose of purchasing plaintiff's stock they were willing to consider that the book value was $360,000; that said value had no relation to any figure placed on Hartsville stock to be paid by U. S. Industries; that no separate value was established for the Hartsville Corporation either in the negotiations or the documents. He emphasized the fact that payment by U. S. Industries was not in cash, which plaintiff received, but in U. S. Industries stock; that restrictions were placed upon the sale of that stock in the hands of the sellers; and that the only assured payment was the $4,867,000, in stock issued June 25, 1968.

The learned Chancellor held that any statute of limitations applicable had been tolled because plaintiff had not discovered the fraud until a few months before the complaint was filed. He found that a fraud had been perpetrated on plaintiff and entered judgment for $34,800 plus interest.

The Court of Appeals reversed finding T.C.A. §28-305, the three (3) year statute of limitations for tortious property damage, to be applicable and not tolled because plaintiff had not exercised reasonable diligence in attempting to discover the fraud. We agree with the results reached by the Court of Appeals on both issues.

Plaintiff testified that Schulder showed him brochures from U. S. Industries, but admitted that he made no inquiry about any of the details of the proposed sale to that company. Plaintiff made no effort to show that he could not have obtained the full facts about the sale before it was consummated or immediately thereafter. The stock of U. S. Industries, Inc. was traded on the New York Stock Exchange in 1968. A full and complete description of the transaction between U. S. Industries and Consolidated Merchandising Corporation was filed with the Exchange. We cannot escape the conclusion that the fraud alleged by plaintiff was not of such a character as to conceal itself and that all of the facts upon which he relies in this case have been available to him, upon reasonable inquiry, continuously since June, 1968.

The applicable rules were stated by the Court of Appeals.

> "Mere ignorance and failure of the plaintiff to discover the existence of a cause of action is not sufficient to toll the running of the statute of limitations. *Hall v. DeSaussure*, [41 Tenn.App. 572, 297 S.W.2d 81 (1956)], and numerous cases. There is an exception to this rule. Fraudulent concealment of the cause of action by the defendant tolls the statute of limitations. It begins to run as of the time of the discovery of the fraud by the plaintiff. *Boro v. Hidell*, 122 Tenn. 80, 120 S.W. 961 (1909); *Bodne v. Austin*, [156 Tenn. 353, 2 S.W.2d 100 (1928)]; *Howell v. Davis*, [43 Tenn.App. 52, 306 S.W.2d 9 (1957)]; and numerous cases. To come within this exception, the plaintiff must prove that the defendant took affirmative action to conceal his cause of action and that he, the plaintiff, could not have discovered his cause of action despite exercising reasonable diligence. *Redwood v. Raskind*, 49 Tenn.App. 69, 350 S.W.2d 414 (1961); *Hudson v. Shoulders*, 164 Tenn. 70, 45 S.W.2d 1072 (1932); *Woodfolk v. Marley*, 39 S.W. 747 (Tenn.Ch.App. 1896), aff. 98 Tenn. 467, 40 S.W. 479 (1897); *Patten v. Standard Oil Co. of Louisiana*, 165 Tenn. 438, 55 S.W.2d 759 (1933); *Ray v. Scheibert*, 224 Tenn. 99, 450 S.W.2d 578 (1959); see 51 Am. Jur.2d, Limitations of Actions, §148 pp. 719-720."

At various stages of this litigation, the parties have relied upon each of five (5) possible statutes of limitations; T.C.A. §28-304, the one (1) year statute of limitations for tortious personal injury; T.C.A. §28-305, the three (3) year statute of limitations for tortious property damage which was applied by the Court of Appeals; T.C.A. §28-309, the six (6) year statute of limitations for contract; T.C.A. §47-2-725, the Tennessee Commercial Code statute of limitations for sales and T.C.A. §28-310, the ten (10) year statute for all cases not expressly provided for.[2]

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[2] T.C.A. §48-1652 effective May 28, 1975, not applicable to the instant case, provides a two (2) year statute of limitations governing the type of action involved herein.

The applicable statute of limitations in a particular cause will be determined according to the gravamen of the complaint. *Swauger v. Maury & Smith Contractors, Inc.*, 512 S.W.2d 261, 262 (Tenn.1974); *Carney v. Smith*, 222 Tenn. 472, 437 S.W.2d 246 (1969); *Brown v. Dunstan*, 219 Tenn. 291, 409 S.W.2d 365 (1966).

In this determination it is important to distinguish this transaction from the more typical situations where corporate directors or officers with inside information purchase or sell stock detrimentally to stockholders at large. In this state and the majority of jurisdictions the common law imposed no fiduciary duties on directors or officers with regard to trading stock with general stockholders. It was said that directors could trade as if outsiders. *Shaw v. Cole Mfg. Co.*, 132 Tenn. 210, 177 S.W. 479 (1915); 2A *Fletcher Cyclopedia Corporations* §1168.1, 283 (1975).[3] Actions based on such fiduciary breaches, if allowed, would be quasi-contractual in nature and thus the six (6) year statute would be applicable. *Wallace v. Lincoln Savings Bank*, 89 Tenn. 630, 15 S.W. 448 (1891).

However, the gravamen of the present case is fraud in the inducement of a contract, the old common law action of deceit. Plaintiff alleges damages resulting from face to face misrepresentations of material facts which induced him to sell his stock at a much lower figure than reasonable. He bases his prayer for $34,800 damages solely on and as a proximate result of defendant's misrepresentations.

An individual induced by fraud to enter into a contract may elect between two remedies. He may treat the contract as voidable and sue for the equitable remedy of rescission or he

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[3] The harshness of this rule has resulted in various statutory provisions prohibiting or regulating inside trading. See T.C.A. §48-1601 et seq.; The Securities Act of 1933, 15 U.S.C.A. §77 et seq. and The Securities Exchange Act of 1934, 15 U.S.C.A. §78 et seq.

may treat the contract as existing and sue for damages at law under the theory of "deceit." The latter is grounded in tort.

> "Thus, a person who has been injured by the fraud of another or others, by either a party or parties to a transaction or a third party or third parties committing fraudulent acts involving or bringing about the negotiation of a transaction, such transaction usually but not necessarily involving business or commercial dealings, may maintain an action at law in tort or recover damages for the injury received from the fraud and deceit perpetrated by such other or others. The foundation of the action is not contract, but tort."
>
> 37 Am.Jur.2d Fraud and Deceit §332 at 439.

Tennessee Code Annotated §28-305 provides as follows:

> "28-305. *Property tort actions—Statutory liabilities—Alienation of affections.*—Actions for injuries to personal or real property, actions for the detention or conversion of personal property, civil actions based upon the alleged violation of any federal or state statute creating monetary liability for personal services rendered, or liquidated damages or other recovery therefor, when no other time of limitation is fixed by the statute creating such liability, and actions for alienation of affections, shall be commenced within three (3) years from the accruing of the cause of action."

It is urged upon us that, in substance, the alleged fraudulent misrepresentation as to expectation of profitability, or to value of a stock, that results in monetary loss cannot be considered an "injury to property" in the classic tort sense of the word.

This argument is predicated upon a narrow definition of the word "injury" as used in the property tort actions three (3) year statute, and the notion that torts, in the classic sense, result only in physical damage.

Injury is defined in Black's Law Dictionary, Revised Fourth Edition as:

> "*INJURY.* Any wrong or damage done to another, either in his person, rights, reputation, or property. Woodruff v. Mining Co., C.C.Cal., 18 F. 781; Hitch v. Edgecommbe County, 132 N.C. 573, 44 S.E. 30. . . .
>
> The words 'damage,' 'loss,' and 'injury' are used interchangeably, and, within legislative meaning and judicial interpretation, import the same thing. In re City of Pittsburgh, 90 A. 329, 331, 243 Pa. 392, 52 L.R.A., N.S., 262."

In *Brown v. Dunstan, supra,* this Court rejected the contention that injury to the person in T.C.A. §28-304 is limited to bodily injury. In doing so the Court expressly approved the rationale in Commerce Oil Refining Corporation v. Miner, 199 A.2d 606 (R.I.1964) and quoted the following from said opinion:

> "The issue presented to us for decision clearly points up the ambiguity of the statutory language 'injuries to the person.'
>
> ***did the legislature contemplate applying the two-year limitation to actions arising from bodily or physical injuries only or to apply it broadly to actions brought to recover damages arising out of the restriction, invasion, or impairment of rights and privileges which are personal to the suiter?
>
> * * * * * *
>
> It is then our conclusion that the phrase 'injuries to the person' as used in the instant statute is to be construed comprehensively and as contemplating its application to actions involving injuries that are other than physical. Its purpose is to include within that period of limitation ac-

> tions brought for injuries resulting from invasions of rights that inhere in man as a rational being, that is, rights to which one is entitled by reason of being a person in the eyes of the law. Such rights, of course, are to be distinguished from those which accrue to an individual by reason of some peculiar status or by virtue of an interest created by contract or property. 199 A.2d 606."
>
> 219 Tenn. at 294, 295.

Brown alleged that defendants had entered into a conspiracy to defraud and discredit him and oust him from his position with First Trust Company and that as a result of specified wrongful acts he had been reduced from his former status in the business and civic world of Chattanooga to one of abject pauperism and rendered incapable of regaining his former wealth or earning a living. The Court held that the gravamen of the action was damages to the plaintiff's reputation as a businessman, father and respected man of society and that such damages are included within "for injury to the person" as that phrase is used in T.C.A. §28-304. Brown's cause of action was held to be barred by the one (1) year statute.

We deem it appropriate to apply the rationale of *Brown* to the property tort action statute. We reject the notion that injury to property as contemplated therein is limited to physical injury to property. In our opinion, the loss in value sustained by plaintiff from the alleged tort of fraud and deceit is included within the phrase, "injuries to personal property" as contemplated in T.C.A. §28-305.

We note that a similar result was reached by this Court in *Budget Rent—A-Car of Knoxville, Inc. v. Car Serv., Inc.*, 469 S.W.2d 360 (Tenn.1971). The complainants alleged a conspiracy which was said to have forced the sale of their business to their loss and damage. Defendants relied upon the three (3) year statute of limitations applicable to property tort actions. The court sustained that defense, and without extensive analysis

said: "Conspiracy is a tort and is subject to the running of the statute of three years." 469 S.W.2d at 362.

There is respectable judicial authority in other states, whose statutes of limitation are similar to ours, that would result in application of the six (6) year statute, and others the ten (10) year statute. We have read all of the cases and given consideration to all of the excellent arguments in the briefs of the parties and those of the two (2) amici curiae. We readily concede that a close question is presented between the choice of the three (3) year statute, the six (6) year statute, and the ten (10) year statute. Nevertheless, we are persuaded that the Court of Appeals was correct in applying the three (3) year statute.

The judgment of the Court of Appeals dismissing plaintiff's action is affirmed. Costs are assessed against plaintiff, Woodson Vance.

Wm. H. D. Fones
Justice

Concur:

Cooper, C.J.
Brock, Harbison, JJ.

Henry, J., not participating

APPENDIX H

CHAPTER 14

MUNICIPAL SECURITIES ACT

9-1401. Short title.—This chapter shall be known and may be cited as the "Tennessee Municipal Securities Act of 1972." [Acts 1972 (Adj. S.), ch. 765, § 1.]

9-1402. Definitions.—As used in this chapter, unless the context otherwise requires:

(a) "Board" shall mean the Tennessee municipal securities board.

(b) "Commissioner" means the commissioner of the state department of insurance.

(c) "Department" means the department of insurance of the state of Tennessee.

(d) "Agent" means any individual other than a broker-dealer who represents a broker-dealer in effecting or attempting to effect purchases or sales of municipal securities for the account of others or for his own account.

(e) "Broker-dealer" or "underwriter-dealer" means any person engaged in the business of effecting transactions in municipal securities for the account of others or for his own account. "Broker-dealer" or "underwriter-dealer" does not include (1) an agent, (2) a municipality, (3) a lawyer, accountant, architect or engineer, employed and acting solely in his professional capacity by an underwriter-dealer, financial consultant, or municipality, or (4) a person who has no place of business in this state if he effects transactions in this state exclusively with or through the municipal corporations issuing the municipal securities involved in the transactions, or underwriter-dealers, (5) a bank, savings institutions, trust companies, insurance companies, investment companies, pension or profit sharing trusts,

or other financial institutions or institutional buyers who effect transactions in municipal securities exclusively from their investment portfolios; provided, however, that any bank which offers municipal securities for sale to the public or to other commercial banks or to other financial institutions in other than casual transactions shall be a broker-dealer, and casual transaction shall be determined by the board, (6) such other persons not within the intent of this paragraph as the board may by rule or order designate.

(f) "Fraud," "deceit," and "defraud" are not limited to common law deceit.

(g) "Prohibited practices." The following shall be prohibited practices and shall be unlawful under the terms of this chapter:

(1) For any person knowingly to subscribe to, or make or cause to be made, any material false statement or representation in any application, financial statement or other document or statement required to be filed under any provision of this chapter; or

(2) For any person, in connection with any transaction or transactions in this state which involve any offer to sell or to buy municipal securities, or any sale or purchase of municipal securities, or advising municipalities with regard to financing municipal projects, either directly or indirectly, (a) to employ any device, scheme or artifice to defraud, or (b) to engage in any act, practice, transaction or course of business which operates or would operate as a fraud or deceit upon the purchaser or seller, or the municipality.

(h) "Financial consultant," "fiscal agent" or "municipal finance consultant" means any person engaged in the business of advising municipalities in this state as to the method of financing municipal projects, and assisting municipalities in the marketing of municipal securities, whether or not such function is carried out as an adjunct to a business primarily conducted as

an underwriter-dealer, or as an adjunct to any other business or profession, but shall not mean any lawyer, accountant or engineer employed and acting solely in his professional capacity by a municipality, financial consultant or underwriter-dealer.

(i) "Person" means an individual, a corporation, a partnership, an association, a joint-stock company, a trust where the interests of the beneficiaries are evidenced by a security, an unincorporated organization, a government, or a political subdivision of a government.

(j)(1) "Sale" or "sell" includes every contract of sale of, contract to sell, or disposition of, a security or interest in a security for value.

(2) "Offer" or "offer to sell" includes every attempt or offer to dispose of, or solicitation of an offer to buy, a municipal security or interest in a municipal security for value.

(3) Any municipal security given or delivered with, or having a bonus on account of, any purchase of municipal securities or any other thing is considered to constitute part of the subject of the purchase and to have been offered and sold for value.

(k) "Municipality" or "municipal corporation" means the state of Tennessee, its agencies, bureaus, commissions, departments or instrumentalities, and any county, incorporated city or town, school district, utility district, sanitary district, power district, industrial development corporation, health and educational facilities board, public building authority, metropolitan form of government, or other municipal or quasi-municipal, or governmental body or political subdivision of the state, now or hereafter created, and having the power to authorize and issue securities.

(l) "Municipal security" means any note, warrant, certificate, bond, debenture, evidence of indebtedness, or, in general, any interest or instrument commonly known as a "security," issued by a municipality as herein defined, or by any state, territory,

possession or protectorate of the United States or any county, city, incorporated town, district, authority or other municipal, quasi-municipal or governmental body or political subdivision thereof. [Acts 1972 (Adj. S.), ch. 765, § 2.]

9-1421. Financial liability arising out of fraudulent practices.—(a) Any person who engages in fraudulent practice or practices in the manner set out in the definition section hereof shall be liable to the person purchasing the municipal security or securities for any loss incurred and such purchaser may sue, either at law or in equity, to recover the consideration paid for such security together with interest at the rate of eight per cent (8%) per year from the date of payment, costs, reasonable attorney's fees or for damages if he no longer owns such security.

(b) Any person who engages in fraudulent practice or practices in the manner set out in the definition section hereof shall be liable to the municipal corporation by which such person is employed for any damages incurred by such municipality by reason of such practices. Such municipal corporation shall have the right to rescind any consulting contract upon a finding by the board of a violation of the provisions of said sections. In the application of this section, "persons," in the case of a corporation, partnership, or association, shall be understood to include both the corporation, partnership, or association, shall be understood to include both the corporation, partnership, or association, and the officer, director or partner thereof who has engaged in such fraudulent, dishonest or unethical practices. [Acts 1972 (Adj.S.), ch. 765, § 21.]

APPENDIX I

28-304. Personal tort actions—Malpractice of attorneys—Civil rights actions—Statutory penalties.—Actions for libel, for injuries to the person, false imprisonment, malicious prosecution, criminal conversation, seduction, breach of marriage promise, actions and suits against attorneys for malpractice whether said actions are grounded or based in contract or tort, civil actions for compensatory or punitive damages, or both, brought under the federal civil rights statutes, and actions for statutory penalties shall be commenced within one (1) year after cause of action accrued. For the purpose of this section, insofar as products liability cases are concerned, the cause of action for injury to the person shall accrue on the date of the personal injury not the date of the negligence or the sale of a product and in said products cases no person shall be deprived of his right to maintain his cause of action until one (1) year from the date of his injury and under no circumstances shall his cause of action be barred before he sustains an injury. [Code 1858, § 2772 (deriv. Acts 1715, ch. 27 § 5); Shan., § 4469; mod. Code 1932, § 8595; Acts 1967, ch. 283, § 1; 1969, ch. 28, § 1; 1969, ch. 293, §§ 1, 2; 1972, ch. 669, § 1.]

28-305. Property tort actions—Statutory liabilities—Alienation of affections.—Actions for injuries to personal or real property, actions for the detention or conversion of personal property, civil actions based upon the alleged violation of any federal or state statute creating monetary liability for personal services rendered, or liquidated damages or other recovery therefor, when no other time of limitation is fixed by the statute creating such liability, and actions for alienation of affections, shall be commenced within three (3) years from the accruing of the cause of action. [Code 1858, § 2773 (deriv. Acts 1715, ch. 27, § 5); Shan., § 4470; Code 1932, § 8598; Acts 1945, ch. 130, § 1; mod. C. Supp. 1950, § 8598.]

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

WALTER PODROG AND J. FRANK MANNING
Class Representatives, Grand Junction Bondholder Class
(Fabricating, Inc.)

Petitioners,

v.

WARING, COX, JAMES, SKLAR & ALLEN,
Attorneys, a partnership,

Respondents.

RESPONSE TO THE PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF TENNESSEE

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REASONS FOR DENYING PETITION FOR WRIT OF CERTIORARI

I. The Federal Question Sought To Be Raised Through This Petition Was Not Properly Raised At Any Level In The Proceedings In The State Courts.

Petitioners raise as the federal question sought to be reviewed the constitutionality of the application of Tennessee Code Annotated §28-304 (now Tennessee Code Annotated §28-3-104) to the facts of this cause. That question has never been properly raised at any stage of the proceedings by Petitioners. It cannot, therefore, now be raised in this Petition.

Although your Respondents cited that specific statute of limitations in question (Tennessee Code Annotated §28-304) as a defense in its initial answer to the Petitioners' Complaint, the allegedly unconstitutional application of that statute was not raised at the trial court by Petitioners; nor was it raised by Petitioners in the Tennessee Court of Appeals when that Court of Appeals reversed and dismissed the judgment rendered in favor of Petitioners in the trial court. That dismissal was based upon the applicability of the same statute of limitations, T.C.A. §28-304. See appendix to Petition, at p. A-17 *et seq.* As is pointed out in Petitioners' Petition at page 5, Petitioners did for the first time specifically attempt to raise in written briefs and argument filed with the Supreme Court of Tennessee the constitutional question they here seek to have this Court review. That constitutional question, however, was not properly raised before the Supreme Court of Tennessee because Petitioners did not comply with Tennessee Code Annotated §29-14-107(b), which provides:

> In any proceeding which involves the validity of a municipal ordinance or franchise, such municipality shall be made a party, and shall be entitled to be heard, and if the statute, ordinance, or franchise is of state wide effect *and is alleged to be unconstitutional, the attorney general of the state shall also be served with a copy of the proceeding and be entitled to be heard.* (Emphasis supplied.)

Further, Tennessee Rules of Civil Procedure Rule 24.04 provides:

> *Notice To Attorney General When Statute, Rule or Regulation Is Questioned.* When the validity of a statute of this State or an administrative rule or regulation of this State is drawn in question in any

> action to which the State or an officer or agency is not a party, the Court shall require that notice be given the attorney general, specifying the pertinent statute, rule or regulation.

Further, Tennessee Rules of Appellate Procedure Rule 32(a) provides:

> *Service; When Required.* When the validity of a statute of this state or an administrative rule or regulation of this state is drawn in question in any appeal to which the state or an office or agency is not a party, the party raising such question shall serve a copy of his brief on the Attorney General.

The record is devoid of any such notice, and counsel for Respondents does not recall any being given.

This notice provision is held to be mandatory, the object of the requirement being to protect the public should the parties be indifferent to the result, as it might affect the public welfare. *Cummings v. Shipp*, 156 Tenn. 595, 3 S.W.2d 1062 (1928).

The Supreme Court of the United States has consistently held that constitutional questions involving the validity of state laws cannot be raised for the first time upon a writ of certiorari. 28 U.S.C. §1257. *Cardinale v. Louisiana*, 394 U.S. 437, 89 S.Ct. 1161, 22 L.Ed.2d 398 (1969).

Thus, Petitioners' contention that "the Tennessee Supreme Court has therefore repeatedly been confronted with this federal constitutional question" ignores the requirement of notice to the attorney general. Failure to comply with this mandatory provision is a jurisdictional error which prohibits the constitutional question from being considered by the Tennessee Supreme Court. *Cummings v. Shipp, supra.* Petitioners' contention is therefore not supported by Tennessee statutory and decisional law.

This Court has specifically held that 28 U.S.C. §1257 "vested this Court with no jurisdiction unless a federal question was raised and decided in the state court below". *Cardinale v. Louisiana, supra.* If it does not appear upon the record that the federal question was both raised and decided in the state court below, the appellate jurisdiction fails. *Cardinale v. Louisiana, supra.*

See also, Street v. New York, 394 U.S. 576, 89 S.Ct. 1354, 22 L.Ed.2d 572 (1969):

> Moreover, this Court has stated that when, as here, the highest state court has failed to pass upon a federal question, it will be assumed that the omission was due to want of proper presentation in the state courts, unless the aggrieved party in this court can affirmatively show the contrary.
>
> 394 U.S. at 582, 89 S.Ct. at 1360.

The burden therefore of demonstrating that the equal protection issue attempted to be raised in this Petition for a Writ of Certiorari was properly raised before the Tennessee Supreme Court rests with the Petitioners. Your Respondent respectfully asserts that the issue was not properly raised in the State Courts of Tennessee; and that therefore this Honorable Court is without jurisdiction to hear this case. Nowhere in either the original opinion of the Supreme Court of Tennessee nor in its opinion on Petition to Rehear does that Court indicate that it has reviewed and passed upon the constitutional question.

It is therefore respectfully submitted that there is an absence in the record of a showing "that the federal question was timely and properly raised so as to give this Court jurisdiction to review the judgment on writ of certiorari." Rules of the Supreme Court of the United States, Rule 21.1(h).

II. The Issues Raised In This Petition For A Writ Of Certiorari Do Not Constitute An Important Question Of Federal Law Which Should Be Settled By This Court.

One of the considerations governing review on certiorari is a finding that a state court has decided an *important question of federal law* that has not been but should be settled by the United States Supreme Court. See Rules of the Supreme Court of the United States, Rule 17.1(c). This Petition for a Writ of Certiorari does not raise such a question.

This Honorable Court has on at least two previous occasions dismissed appeals from state courts as not presenting a substantial federal question where the state courts have upheld the constitutionality of legislation which created statutes of limitations of a shorter period of time for particular professions or trades than statutes of limitations applicable to non-members of those professions and trades.

In *Carter v. Hartenstein*, 248 Ark.1172, 455 S.W.2d 918 (1970), plaintiff contended that the four-year statute of limitations applicable to those engaged in the designing, planning, supervising or observing construction or construction and repair of an improvement to real estate violated the 14th Amendment to the United States Constitution, was discriminatory, was applied in violation of the equal protection of the laws, and constituted special legislation. The Supreme Court of Arkansas upheld the constitutionality of this specialized statute of limitations, and this Honorable Court dismissed the appeal "for want of a substantial federal question." *Carter v. Hartenstein*, 401 U.S. 901, 91 S.Ct. 868, 27 L.Ed.2d 800 (1971).

Likewise, in *Woodward v. Burham City Hospital*, 79 Ill.2d 295, 402 N.E.2d 560 (1979), the Illinois two-year statute of limitations for suits against physicians and hospitals based on medical malpractice was upheld by the Illinois Supreme Court against attacks based upon the due process and equal protection clauses of the United States Constitution as well as other attacks which raised questions identical to those raised by Petitioners in this cause. Once again, this Court held that the attempted appeal by those contending that the two-year statute of limitations applicable to a particular class of professionals was violative of the equal protection clause did not raise a substantial federal question. *Woodward v. Burham City Hospital*, 449 U.S. 807, 101 S.Ct. 54, 66 L.Ed.2d 11 (1980).

Since this Court has previously held that the identical issues raised by Petitioners in this cause do not involve substantial federal questions, it is respectfully submitted that the Petition in this cause should be denied as not raising "an important question of federal law which has not been but should be settled by this Court."

CONCLUSION

The record in this cause fails to support Petitioners' contention that the constitutional question has been properly raised before any state court which heard the issues in this cause. This failure precludes Petitioners' raising it at this level and obviates jurisdiction to grant the Writ of Certiorari.

Further, prior decisions by this Court have indicated that the question raised in this Petition does not constitute a substantial federal question, thus eliminating the only real consideration set out in Rule 17 of this Court's

rules for considering the granting of certiorari in this cause.

For both of those reasons, it is respectfully submitted that the Writ of Certiorari should be denied.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that I have forwarded the required number of printed copies of this Response to the Clerk of the United States Supreme Court and to counsel For Petitioners: Frank B. Bird, P.O. Box 647, Maryville, Tennessee 37803-0647, and H. Morris Denton, P.O. Box 306, Bolivar, Tennessee 38008 all on this 1st day of November, 1984.

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No. 84-560

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PETITIONER'S REPLY BRIEF PURSUANT TO RULE 22.5, ADDRESSED TO ARGUMENTS FIRST RAISED IN RESPONDENTS' BRIEF IN OPPOSITION

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Respondent's first contend that the Attorney General of Tennessee should have been notified of the proceedings in the state courts.

The various requirements cited by Respondents to the effect that the Attorney General be notified of the state court proceedings apply only where there is a claim that the statute involved is unconstitutional; Petitioners have never contended that the statutes in question (T.C.A. §28-304 and T.C.A. §28-305) are unconstitutional; rather, Petitioners' contention is that the Tennessee Supreme Court in applying said statutes to the case at bar has grafted judicially created amendments on to them to give unwarranted and constitutionally impermissible special privileges to attorneys: — namely, being free from suit

after one year, even though non-attorneys, for the same violation of a securities fruad statute, are not free until after three years.

It follows that since Petitioners have never contended that the statutes in question are unconstitutional, there is no merit to Respondents' argument that the Petition should be dismissed for failure to notify the Tennessee Attorney General of the state court proceedings.

The second argument advanced by Respondents, that there is no important federal question involved, is equally without merit. Nothing is more important to this Court and the Nation than that this Court stand as the ultimate guardian of the right of every citizen to the equal protection of the law. This Court cannot correct every denial of equal protection, but where the denial results in special privilege for attorneys, who are officers of the Court, it is especially important that this Court intervene.

Respectfully submitted,

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